UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(MarkOne)

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

For the Quarterly Period Ended June 30, 2006

Or

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

For the transition period from to

Commission File No. 1-6639

MAGELLAN HEALTH SERVICES, INC.
(Exact name of registrant as specified in its charter)

Delaware 58-1076937
(State of other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

55 Nod Road, Avon, Connecticut 06001
(Address of principal executive offices) (Zip code)

(860) 507-1900
(Registrant’s telephone number, including area code)

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

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

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 twelve 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 ☒ No ☐

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

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐

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

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PRECEDING FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes ☒ No ☐

The number of shares of the registrant’s Ordinary Common Stock outstanding as of June 30, 2006 was 37,148,742.
## FORM 10-Q

MAGELLAN HEALTH SERVICES, INC. AND SUBSIDIARIES

## INDEX

**PART I—Financial Information:**

<table>
<thead>
<tr>
<th>Item</th>
<th>Financial Statements</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Condensed Consolidated Balance Sheets—December 31, 2005 and June 30, 2006</td>
</tr>
<tr>
<td></td>
<td>Condensed Consolidated Statements of Income—For the Three Months and Six Months Ended June 30, 2005 (restated) and 2006</td>
</tr>
<tr>
<td></td>
<td>Condensed Consolidated Statements of Cash Flows—For the Six Months Ended June 30, 2005 (restated) and 2006</td>
</tr>
<tr>
<td></td>
<td>Notes to Condensed Consolidated Financial Statements</td>
</tr>
</tbody>
</table>

| Item 2 | Management’s Discussion and Analysis of Financial Condition and Results of Operations |
| Item 3 | Quantitative and Qualitative Disclosures About Market Risk |
| Item 4 | Controls and Procedures |

**PART II—Other Information:**

| Item 1 | Legal Proceedings |
| Item 2 | Unregistered Sales of Equity Securities and Use of Proceeds |
| Item 3 | Defaults Upon Senior Securities |
| Item 4 | Submission of Matters to a Vote of Security Holders |
| Item 5 | Other Information |
| Item 6 | Exhibits |

**Signatures**
PART I—FINANCIAL INFORMATION

Item 1. Financial Statements.

MAGELLAN HEALTH SERVICES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except per share amounts)

<table>
<thead>
<tr>
<th>Year</th>
<th>Assets</th>
<th>Liabilities</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total Current Assets</td>
<td>Total Current Liabilities</td>
</tr>
<tr>
<td>December 31, 2005</td>
<td>$540,777</td>
<td>$311,925</td>
</tr>
<tr>
<td>June 30, 2006</td>
<td>$509,226</td>
<td>$294,642</td>
</tr>
</tbody>
</table>

See accompanying notes to condensed consolidated financial statements.
## MAGELLAN HEALTH SERVICES, INC. AND SUBSIDIARIES
### CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)
(In thousands, except per share amounts)

<table>
<thead>
<tr>
<th></th>
<th>Three Months Ended June 30</th>
<th>Six Months Ended June 30</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2005 (restated)</td>
<td>2006</td>
</tr>
<tr>
<td>Net revenue</td>
<td>$464,544</td>
<td>$398,933</td>
</tr>
<tr>
<td>Cost and expenses:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of care</td>
<td>316,921</td>
<td>262,706</td>
</tr>
<tr>
<td>Direct service costs and other operating expenses</td>
<td>90,201</td>
<td>86,104</td>
</tr>
<tr>
<td>Equity in earnings of unconsolidated subsidiaries</td>
<td>(1,503)</td>
<td>—</td>
</tr>
<tr>
<td>Depreciation and amortization</td>
<td>13,573</td>
<td>11,333</td>
</tr>
<tr>
<td>Interest expense</td>
<td>8,611</td>
<td>1,721</td>
</tr>
<tr>
<td>Interest income</td>
<td>(3,899)</td>
<td>(4,921)</td>
</tr>
<tr>
<td>Stock compensation expense</td>
<td>4,419</td>
<td>6,594</td>
</tr>
<tr>
<td>Gain on sale of assets</td>
<td>—</td>
<td>(403)</td>
</tr>
<tr>
<td></td>
<td>428,323</td>
<td>363,134</td>
</tr>
<tr>
<td>Income from continuing operations before income taxes and minority interest</td>
<td>36,221</td>
<td>35,799</td>
</tr>
<tr>
<td>Provision for income taxes</td>
<td>15,316</td>
<td>15,575</td>
</tr>
<tr>
<td>Income from continuing operations before minority interest</td>
<td>20,905</td>
<td>20,224</td>
</tr>
<tr>
<td>Minority interest, net</td>
<td>4</td>
<td>—</td>
</tr>
<tr>
<td>Income from continuing operations</td>
<td>20,901</td>
<td>20,224</td>
</tr>
<tr>
<td>Income from discontinued operations (1)</td>
<td>816</td>
<td>—</td>
</tr>
<tr>
<td>Net income</td>
<td>21,717</td>
<td>20,224</td>
</tr>
<tr>
<td>Other comprehensive (loss) income</td>
<td>(458)</td>
<td>166</td>
</tr>
<tr>
<td>Comprehensive income</td>
<td>$21,259</td>
<td>$20,390</td>
</tr>
<tr>
<td>Weighted average number of common shares outstanding—basic (See Note D)</td>
<td>35,567</td>
<td>36,999</td>
</tr>
<tr>
<td>Weighted average number of common shares outstanding—diluted (See Note D)</td>
<td>36,980</td>
<td>38,599</td>
</tr>
<tr>
<td>Income per common share—basic:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income from continuing operations</td>
<td>$0.59</td>
<td>$0.55</td>
</tr>
<tr>
<td>Income from discontinued operations</td>
<td>$0.02</td>
<td>$0.00</td>
</tr>
<tr>
<td>Net income</td>
<td>$0.61</td>
<td>$0.55</td>
</tr>
<tr>
<td>Income per common share—diluted:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income from continuing operations</td>
<td>$0.57</td>
<td>$0.52</td>
</tr>
<tr>
<td>Income from discontinued operations</td>
<td>$0.02</td>
<td>$0.00</td>
</tr>
<tr>
<td>Net income</td>
<td>$0.59</td>
<td>$0.52</td>
</tr>
</tbody>
</table>

(1) Net of income tax provision of $940 and $1,045 for the three months and six months ended June 30, 2005, respectively.

See accompanying notes to condensed consolidated financial statements.

4
MAGELLAN HEALTH SERVICES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED JUNE 30,
((Unaudited)
(In thousands)

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Cash flows from operating activities:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net income</td>
<td>$44,811</td>
<td>$42,539</td>
</tr>
<tr>
<td>Adjustments to reconcile net income to net cash from operating activities:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gain on sale of assets</td>
<td>—</td>
<td>(5,148)</td>
</tr>
<tr>
<td>Depreciation and amortization</td>
<td>24,791</td>
<td>21,990</td>
</tr>
<tr>
<td>Equity in earnings of unconsolidated subsidiaries</td>
<td>(2,952)</td>
<td>(390)</td>
</tr>
<tr>
<td>Non-cash interest expense</td>
<td>694</td>
<td>694</td>
</tr>
<tr>
<td>Non-cash stock compensation expense</td>
<td>8,169</td>
<td>12,094</td>
</tr>
<tr>
<td>Non-cash income tax expense</td>
<td>30,754</td>
<td>30,116</td>
</tr>
<tr>
<td><strong>Cash flows from changes in assets and liabilities, net of effects from acquisitions of businesses:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Restricted cash</td>
<td>(46,030)</td>
<td>(11,627)</td>
</tr>
<tr>
<td>Accounts receivable, net</td>
<td>12,578</td>
<td>6,878</td>
</tr>
<tr>
<td>Other assets</td>
<td>169</td>
<td>(3,336)</td>
</tr>
<tr>
<td>Accounts payable and accrued liabilities</td>
<td>(3,281)</td>
<td>(20,481)</td>
</tr>
<tr>
<td>Medical claims payable and other medical liabilities</td>
<td>19,929</td>
<td>(1,970)</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>153</td>
<td>(53)</td>
</tr>
<tr>
<td>Minority interest, net of dividends paid</td>
<td>123</td>
<td>(1,520)</td>
</tr>
<tr>
<td>Other</td>
<td>344</td>
<td>39</td>
</tr>
<tr>
<td><strong>Net cash provided by operating activities</strong></td>
<td>90,252</td>
<td>69,825</td>
</tr>
</tbody>
</table>

| **Cash flows from investing activities:** |            |            |
| Capital expenditures              | (8,628)    | (8,923)    |
| Proceeds from sale of assets      | —          | 22,200     |
| Purchase of investments           | (224,683)  | (23,481)   |
| Maturity of investments           | 173,777    | 206,534    |
| Acquisitions and investments in businesses, net of cash acquired | —         | (120,735)  |
| Proceeds from note receivable     | 7,000      | 3,000      |
| **Net cash (used in) provided by investing activities** | (52,534)   | 78,595     |

| **Cash flows from financing activities:** |            |            |
| Payments on long-term debt and capital lease obligations | (13,560)   | (12,657)   |
| Proceeds from exercise of stock options and warrants | 12,041     | 7,771      |
| **Net cash used in financing activities** | (1,519)    | (4,886)    |
| Net increase in cash and cash equivalents | 36,199     | 143,534    |
| Cash and cash equivalents at beginning of period | 45,390     | 81,039     |
| **Cash and cash equivalents at end of period** | $81,589    | $224,573   |

See accompanying notes to condensed consolidated financial statements.
NOTE A—General

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of Magellan Health Services, Inc., a Delaware corporation ("Magellan"), include the accounts of Magellan, its majority owned subsidiaries, and all variable interest entities ("VIEs") for which Magellan is the primary beneficiary (together with Magellan, the "Company"). The financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the Securities and Exchange Commission’s (the “SEC”) instructions to Form 10-Q. Accordingly, the financial statements do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring adjustments considered necessary for a fair presentation, have been included. The results of operations for the three months and six months ended June 30, 2006 are not necessarily indicative of the results to be expected for the full year. All intercompany accounts and transactions have been eliminated in consolidation.

These unaudited condensed consolidated financial statements should be read in conjunction with the Company’s audited consolidated financial statements for the year ended December 31, 2005 and the notes thereto, which are included in the Company’s Annual Report on Form 10-K filed with the SEC on March 8, 2006.

Restatements of Previously Issued Unaudited Condensed Consolidated Financial Statements

On March 7, 2006, the Company announced that it was restating previously filed financial statements to correct the Company’s accounting for reversals of valuation allowances pertaining to deferred tax assets (excluding deferred tax assets related to the Company’s net operating loss carryforwards) that existed prior to the Company’s emergence from bankruptcy on January 5, 2004. The Company had recorded the reversals of valuation allowances for such deferred tax assets as reductions to the Company’s income tax provision. In accordance with American Institute of Certified Public Accountants (“AICPA”) Statement of Position (“SOP”) 90-7, “Financial Reporting by Entities in Reorganization Under the Bankruptcy Code” (“SOP 90-7”), and the Financial Accounting Standard Board’s Emerging Issues Task Force (“EITF”) Topic No. D-33, “Timing of Recognition of Tax Benefits for Pre-Reorganization Temporary Differences and Carryforwards” (“EITF D-33”), such reversals of valuation allowances should be recorded as reductions to goodwill. Accordingly, the Company has restated its consolidated financial statements for the fiscal year ended December 31, 2004, and for the quarters ended March 31, 2004, June 30, 2004, September 30, 2004, December 31, 2004, March 31, 2005, June 30, 2005 and September 30, 2005. All applicable financial information contained in this Form 10-Q gives effect to these restatements.
The quarterly impacts of the restatement adjustments for the three months and six months ended June 30, 2005 are reflected below (in thousands, except per share amounts):

<table>
<thead>
<tr>
<th></th>
<th>Three months ended</th>
<th>Six months ended</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>June 30, 2005</td>
<td>June 30, 2005</td>
</tr>
<tr>
<td>Net revenue</td>
<td>$ —</td>
<td>$ —</td>
</tr>
<tr>
<td>Cost and expenses:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of care</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Direct service costs and other operating expenses</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Equity in earnings of unconsolidated subsidiaries</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Depreciation and amortization</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Interest expense</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Interest income</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Stock compensation expense</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Gain on sale of assets</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Income from continuing operations before income taxes and minority interest</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Provision for income taxes</td>
<td>434</td>
<td>922</td>
</tr>
<tr>
<td>Income from continuing operations before minority interest</td>
<td>(434)</td>
<td>(922)</td>
</tr>
<tr>
<td>Minority interest, net</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Income from continuing operations</td>
<td>(434)</td>
<td>(922)</td>
</tr>
<tr>
<td>Discontinued operations:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income (loss) from discontinued operations, net of income taxes</td>
<td>(504)</td>
<td>(538)</td>
</tr>
<tr>
<td>Net income</td>
<td>(938)</td>
<td>(1,460)</td>
</tr>
<tr>
<td>Income available to common stockholders</td>
<td>$ (938)</td>
<td>$ (1,460)</td>
</tr>
<tr>
<td>Weighted average number of common shares outstanding—basic</td>
<td>35,567</td>
<td>35,475</td>
</tr>
<tr>
<td>Weighted average number of common shares outstanding—diluted</td>
<td>36,980</td>
<td>36,899</td>
</tr>
<tr>
<td>Income per common share available to common stockholders—basic:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income from continuing operations</td>
<td>$ (0.01)</td>
<td>$ (0.02)</td>
</tr>
<tr>
<td>Income (loss) from discontinued operations</td>
<td>$ (0.02)</td>
<td>$ (0.02)</td>
</tr>
<tr>
<td>Net income</td>
<td>$ (0.03)</td>
<td>$ (0.04)</td>
</tr>
<tr>
<td>Income per common share available to common stockholders—diluted:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income from continuing operations</td>
<td>$ (0.01)</td>
<td>$ (0.02)</td>
</tr>
<tr>
<td>Income (loss) from discontinued operations</td>
<td>$ (0.02)</td>
<td>$ (0.02)</td>
</tr>
<tr>
<td>Net income</td>
<td>$ (0.03)</td>
<td>$ (0.04)</td>
</tr>
</tbody>
</table>

The weighted average number of common shares outstanding, both basic and diluted, are not affected by the restatement.
Summary of Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Significant estimates of the Company include, among other things, accounts receivable realization, valuation allowances for deferred tax assets, valuation of goodwill and intangible assets, medical claims payable, other medical liabilities, stock-based compensation assumptions, tax contingencies and legal liabilities. Actual results could differ from those estimates.

Managed Care Revenue

Managed care revenue is recognized over the applicable coverage period on a per member basis for covered members. Managed care risk revenues approximated $413.3 million and $815.6 million for the three months and six months ended June 30, 2005, respectively and $349.9 million and $702.6 million for the three months and six months ended June 30, 2006, respectively.

Performance-based Revenue

The Company has the ability to earn performance-based revenue under certain risk and non-risk contracts. Performance-based revenue generally is based on either the ability of the Company to manage care for its clients below specified targets, or on other operating metrics. For each such contract, the Company estimates and records performance-based revenue after considering the relevant contractual terms and the data available for the performance-based revenue calculation. Pro-rata performance-based revenue is recognized on an interim basis pursuant to the rights and obligations of each party upon termination of the contracts. Performance-based revenues were $2.7 million and $6.9 million for the three months and six months ended June 30, 2005, respectively, and $3.0 million and $6.6 million for the three months and six months ended June 30, 2006, respectively.

Significant Customers

The Company’s contracts with the State of Tennessee’s TennCare program (“TennCare”) and with subsidiaries of WellPoint, Inc. (“WellPoint”), each generated revenues that exceeded, in the aggregate, ten percent of consolidated net revenues for each of the three months and six months ended June 30, 2005 and 2006. The Company also has a significant concentration of business from individual counties which are part of the Pennsylvania Medicaid program.

The Company provides managed behavioral healthcare services for TennCare, both through contracts held by the Company’s wholly owned subsidiary Tennessee Behavioral Health, Inc. (“TBH”) and through a contract held by Premier Behavioral Health Systems of Tennessee, LLC (“Premier”), a joint venture in which the Company owned a fifty percent interest. In addition, the Company contracts with Premier to provide certain services to the joint venture. The Company consolidates the results of operations of Premier, including revenue and cost of care, in the Company’s consolidated statements of income. On April 11, 2006, the Company purchased the other fifty percent interest in Premier for $1.5 million, so that Premier is now a wholly-owned subsidiary of the Company. TennCare has divided its program into three regions, and the Company’s TennCare contracts, which extend through June 30, 2007, currently encompass all of the TennCare membership for all three regions. The Company recorded revenue of $113.6 million and $226.7 million during the three months and six months ended June 30, 2005, respectively, and $101.8 million and $210.3 million during the three months and six months ended June 30, 2006, respectively, from its TennCare contracts.
On April 7, 2006, TennCare issued a Request for Proposals ("RFP") for the management of the integrated delivery of behavioral and physical medical care to TennCare enrollees in the Middle region by managed care organizations. The RFP states that the start date of any such contract awarded pursuant to the RFP is expected to be April 1, 2007. Because the Company's contracts with TennCare can be terminated by TennCare prior to June 30, 2007, the contract for the Middle region would be terminated should an implementation occur prior to June 30, 2007 of any contract awarded pursuant to the RFP.

On July 26, 2006, TennCare announced the two winning bidders to the RFP process. The Company had not partnered with either of these bidders. For the three months and six months ended June 30, 2006, revenue derived from TennCare enrollees residing in the Middle region amounted to $36.8 million and $77.2 million, respectively.

Total revenue from the Company's contracts with WellPoint approximated $54.6 million and $104.4 million during the three months and six months ended June 30, 2006, respectively. Included in the revenue amount for the three months and six months ended June 30, 2005, respectively, and approximated $51.4 million and $98.4 million during the three months and six months ended June 30, 2006, respectively, included in the revenue amount for the three months and six months ended June 30, 2005, respectively, and approximated $51.4 million and $98.4 million during the three months and six months ended June 30, 2006, respectively, were revenue of $3.8 million and $6.2 million from contracts that National Imaging Associates, Inc. ("NIA") has with WellPoint. As discussed in Note B to the Company's financial statements, the Company and NIA entered into an agreement for NIA's managed behavioral healthcare contracts with WellPoint in June 2005 which extends through December 31, 2007.

The Company derives a significant portion of its revenue from contracts with various counties in the State of Pennsylvania (the "Pennsylvania Counties"). Although these are separate contracts with individual counties, they all pertain to the Pennsylvania Medicaid program. Revenues from the Pennsylvania Counties in the aggregate totaled $54.0 million and $105.5 million in the three months and six months ended June 30, 2005, respectively, and $61.9 million and $124.0 million in the three months and six months ended June 30, 2006, respectively.

The Company recorded net revenue from Aetna, Inc. ("Aetna") of $60.7 million and $122.6 million for the three months and six months ended June 30, 2005, respectively, which represented in excess of ten percent of the consolidated revenues of the Company for such periods. The Company's contract with Aetna terminated on December 31, 2005. During the three months and six months ended June 30, 2006, the Company recognized $0.8 million and $5.4 million of revenue related to the performance of one-time, transitional activities associated with the contract termination.

Cash and Cash Equivalents

Cash equivalents are short-term, highly liquid interest-bearing investments with maturity dates of three months or less when purchased, consisting primarily of money market instruments. The Company records as cash and cash equivalents, excess capital and undistributed earnings for its regulated subsidiaries, which as of June 30, 2006 was $32.5 million.
Restricted Assets

The Company has certain assets which are considered restricted for: (i) the payment of claims under the terms of certain managed behavioral healthcare contracts; (ii) regulatory purposes related to the payment of claims in certain jurisdictions; and (iii) the maintenance of minimum required tangible net equity levels for certain of the Company’s subsidiaries. Significant restricted assets of the Company as of December 31, 2005 and June 30, 2006 were as follows (in thousands):

<table>
<thead>
<tr>
<th></th>
<th>December 31, 2005</th>
<th></th>
<th>June 30, 2006</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Restricted cash</td>
<td>$149,723</td>
<td></td>
<td>$161,600</td>
<td></td>
</tr>
<tr>
<td>Restricted short-term investments</td>
<td>42,976</td>
<td></td>
<td>36,441</td>
<td></td>
</tr>
<tr>
<td>Restricted deposits (included in other current assets)</td>
<td>16,498</td>
<td></td>
<td>20,542</td>
<td></td>
</tr>
<tr>
<td>Restricted long-term investments</td>
<td>2,897</td>
<td></td>
<td>3,512</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>$212,094</td>
<td></td>
<td>$222,095</td>
<td></td>
</tr>
</tbody>
</table>

Investments


As of June 30, 2006, there were no unrealized losses that the Company believed to be other-than-temporary, because the Company believes it is probable that: (i) all contractual terms of each investment will be satisfied, (ii) the decline in fair value is due primarily to changes in interest rates (and not because of increased credit risk), and (iii) the Company intends and has the ability to hold each investment for a period of time sufficient to allow a market recovery. Unrealized losses related to investments greater and less than one year are not material. No realized gains or losses were recorded for the three months and six months ended June 30, 2005 and 2006. The following is a summary of short-term and long-term investments at December 31, 2005 and June 30, 2006 (in thousands):

<table>
<thead>
<tr>
<th></th>
<th>December 31, 2005</th>
<th></th>
<th>Gross Unrealized Gains</th>
<th>Gross Unrealized Losses</th>
<th>Estimated Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Government and agency securities</td>
<td>$63,783</td>
<td></td>
<td>$—</td>
<td>$(158)</td>
<td>$63,625</td>
</tr>
<tr>
<td>Corporate debt securities</td>
<td>175,580</td>
<td></td>
<td></td>
<td>$457</td>
<td>175,123</td>
</tr>
<tr>
<td>Certificates of deposit</td>
<td>302</td>
<td></td>
<td></td>
<td></td>
<td>302</td>
</tr>
<tr>
<td>Total investments at December 31, 2005</td>
<td>$239,665</td>
<td></td>
<td>$—</td>
<td>$(615)</td>
<td>$239,050</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>June 30, 2006</th>
<th></th>
<th>Gross Unrealized Gains</th>
<th>Gross Unrealized Losses</th>
<th>Estimated Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Government and agency securities</td>
<td>$29,852</td>
<td></td>
<td>$—</td>
<td>$(82)</td>
<td>$29,770</td>
</tr>
<tr>
<td>Corporate debt securities</td>
<td>26,554</td>
<td></td>
<td></td>
<td>$(157)</td>
<td>26,397</td>
</tr>
<tr>
<td>Certificates of deposit</td>
<td>270</td>
<td></td>
<td></td>
<td></td>
<td>270</td>
</tr>
<tr>
<td>Total investments at June 30, 2006</td>
<td>$56,676</td>
<td></td>
<td>$—</td>
<td>$(239)</td>
<td>$56,437</td>
</tr>
</tbody>
</table>
The maturity dates of the Company’s investments as of June 30, 2006 are summarized below (in thousands):

<table>
<thead>
<tr>
<th>Due</th>
<th>Amortized Cost</th>
<th>Estimated Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>prior to July 1, 2007</td>
<td>$53,134</td>
<td>$52,925</td>
</tr>
<tr>
<td>July 1, 2007 to April 30, 2008</td>
<td>3,542</td>
<td>3,512</td>
</tr>
<tr>
<td>Total investments at June 30, 2006</td>
<td>$56,676</td>
<td>$56,437</td>
</tr>
</tbody>
</table>

Goodwill

Goodwill is accounted for in accordance with SFAS No. 142, “Goodwill and Other Intangible Assets” (“SFAS 142”). Pursuant to SFAS 142, the Company is required to test its goodwill for impairment on at least an annual basis. The Company has selected October 1 as the date of its annual impairment test. The balance of goodwill of $290.2 million at December 31, 2005 was allocated entirely to the Health Plan segment (as described below). At June 30, 2006, approximately $105.6 million of goodwill was allocated to the Radiology Benefits Management segment (as described below), and the remaining $261.2 million was allocated to the Health Plan segment.

The changes in the carrying amount of Company goodwill for the six months ended June 30, 2006 are reflected in the table below (in thousands):

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount (in thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance as of December 31, 2005</td>
<td>$290,192</td>
</tr>
<tr>
<td>Adjustment to goodwill as a result of the projected realization of pre-emergence deferred tax assets subsequent to fresh-start reporting(1)</td>
<td>(29,019)</td>
</tr>
<tr>
<td>Adjustment to goodwill as a result of the acquisition of NIA—See Note B</td>
<td>105,649</td>
</tr>
<tr>
<td>Balance as of June 30, 2006</td>
<td>$366,822</td>
</tr>
</tbody>
</table>

(1) During fiscal 2006, the Company recorded tax benefits from the utilization of deferred tax assets, including net operating loss carryforwards ("NOLs"), that existed prior to the Company’s emergence from bankruptcy on January 5, 2004. These tax benefits have been reflected as reductions of goodwill in accordance with SOP 90-7.

Intangible Assets

At December 31, 2005 and June 30, 2006, the Company had net identifiable intangible assets (primarily customer agreements and lists and provider networks) of approximately $30.4 million and $39.0 million, respectively, net of accumulated amortization of approximately $17.3 million and $22.2 million, respectively. Intangible assets are amortized over their estimated useful lives, which range from approximately four to eighteen years. Amortization expense was $3.5 million and $6.9 million for the three months and six months ended June 30, 2005, respectively and $2.6 million and $4.9 million for the three months and six months ended June 30, 2006, respectively.

Cost of Care, Medical Claims Payable and Other Medical Liabilities

Cost of care is recognized in the period in which members received managed healthcare services. In addition to actual benefits paid, cost of care includes the impact of accruals for estimates of medical claims payable.
Medical claims payable represents the liability for healthcare claims reported but not yet paid and claims incurred but not yet reported (“IBNR”) related to the Company’s managed healthcare businesses. The IBNR portion of medical claims payable is estimated based on past claims payment experience for member groups, enrollment data, utilization statistics, authorized healthcare services and other factors. This data is incorporated into contract-specific actuarial reserve models. Although considerable variability is inherent in such estimates, management believes the liability for medical claims payable is adequate. Medical claims payable balances are continually monitored and reviewed. Changes in assumptions for cost of care caused by changes in actual experience could cause the estimates to change in the near term. The Company believes that the amount of medical claims payable is adequate to cover its ultimate liability for unpaid claims as of June 30, 2006; however, actual claims payments and other items may differ from established estimates.

Other medical liabilities consist primarily of “reinvestment” payables under certain managed behavioral healthcare contracts with Medicaid customers. Under this type of contract, if the cost of care is less than certain minimum amounts specified in the contract (usually as a percentage of revenue), the Company is required to “reinvest” such difference in behavioral healthcare programs when and as specified by the customer or to pay the difference to the customer for their use in funding such programs.

Income Taxes

The Company’s effective income tax rate was 42.3 percent and 42.7 percent for the three months and six months ended June 30, 2005 (restated), respectively, and 43.5 percent and 43.9 percent for the three months and six months ended June 30, 2006, respectively. The effective rates for the three months and six months ended June 30, 2005 and 2006 differ from federal statutory income tax rates primarily due to state income taxes and permanent differences between book and tax income.

Stock-Based Compensation

At December 31, 2005 and June 30, 2006, the Company had stock-based employee incentive plans, which are described below.

Stock Option Plans

On January 5, 2004, (the “Effective Date”), the Company established the 2003 Management Incentive Plan (“2003 MIP”) which allows for the issuance of up to 6,373,689 shares of common stock pursuant to stock options or stock grants. During fiscal 2004, the Company granted options for the purchase of 4.4 million shares of common stock at a weighted average grant date fair value of approximately $14.61 per share. These options vest ratably on each anniversary date over the three to four years subsequent to grant, and have a 10 year life. During fiscal 2005, the Company granted options for the purchase of 1.1 million shares of common stock at a weighted average grant date fair value of approximately $10.90 per share. These options vest ratably on each anniversary date over the four years subsequent to grant, and have a 10 year life. Other than the 2004 Options (defined below) and certain options granted under the 2006 MIP (defined below), options granted by the Company have exercise prices equal to the fair market value on the date of grant.
Summarized information relative to the Company’s stock options issued under the 2003 MIP for the years ended December 31, 2004 and 2005 is as follows:

<table>
<thead>
<tr>
<th></th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Options</td>
<td>Weighted Average Exercise Price</td>
</tr>
<tr>
<td>Balance, beginning of period</td>
<td>— $ —</td>
<td>4,220,222 $13.34</td>
</tr>
<tr>
<td>Granted</td>
<td>4,402,522</td>
<td>13.34</td>
</tr>
<tr>
<td>Cancelled</td>
<td>(182,300)</td>
<td>16.10</td>
</tr>
<tr>
<td>Exercised</td>
<td>— $ —</td>
<td>13.34</td>
</tr>
<tr>
<td>Balance, end of period</td>
<td>4,220,222 $13.34</td>
<td>4,014,711 $18.50</td>
</tr>
<tr>
<td>Exercisable, end of period</td>
<td>— $ —</td>
<td>30,045 $33.05</td>
</tr>
</tbody>
</table>

The fair values of the stock options granted were estimated on the date of their grant using the Black-Scholes-Merton option pricing model based on the following weighted average assumptions for the years ended December 31, 2004 and 2005:

<table>
<thead>
<tr>
<th></th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk-free interest rate</td>
<td>3.35%</td>
<td>2.97%</td>
</tr>
<tr>
<td>Expected life</td>
<td>5 years</td>
<td>4 years</td>
</tr>
<tr>
<td>Expected volatility</td>
<td>39.10%</td>
<td>37.80%</td>
</tr>
<tr>
<td>Expected dividend yield</td>
<td>0.00%</td>
<td>0.00%</td>
</tr>
</tbody>
</table>

The following table illustrates pro forma net income and pro forma net income per share as if the fair value-based method of accounting for stock options under SFAS No. 123, “Accounting for Stock-Based Compensation” (“SFAS 123”) had been applied in measuring compensation cost for stock-based awards for the three months and six months ended June 30, 2005 (in thousands, except per share data):

<table>
<thead>
<tr>
<th></th>
<th>Three Months Ended</th>
<th>Six Months Ended</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net income, as reported</td>
<td>$21,717 (restated)</td>
<td>$44,811</td>
</tr>
<tr>
<td>Add: Stock-based employee compensation expense included in reported net income, net of related tax effects</td>
<td>4,419</td>
<td>8,169</td>
</tr>
<tr>
<td>Deduct: Total stock-based employee compensation expense determined under fair value method, net of related tax effects</td>
<td>(5,414)</td>
<td>(10,325)</td>
</tr>
<tr>
<td>Pro forma net income</td>
<td>$20,722</td>
<td>$42,655</td>
</tr>
<tr>
<td>Income per common share:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Basic—as reported</td>
<td>$ 0.61</td>
<td>$ 1.26</td>
</tr>
<tr>
<td>Basic—pro forma</td>
<td>$ 0.58</td>
<td>$ 1.20</td>
</tr>
<tr>
<td>Diluted—as reported</td>
<td>$ 0.59</td>
<td>$ 1.21</td>
</tr>
<tr>
<td>Diluted—pro forma</td>
<td>$ 0.56</td>
<td>$ 1.16</td>
</tr>
</tbody>
</table>

On February 24, 2006, the board of directors of the Company approved three equity plans and recommended they be submitted for approval by the Company’s shareholders at the 2006 Annual Meeting.
of Shareholders. The board approved the 2006 Management Incentive Plan (“2006 MIP”), the 2006 Director Equity Compensation Plan (“Director Plan”) and
the 2006 Employee Stock Purchase Plan (“ESPP”). All three of the aforementioned plans were approved by the Company’s shareholders at the 2006 Annual
Meeting of Shareholders on May 16, 2006.

The 2006 MIP, which is similar to the Company’s 2003 MIP, authorizes the issuance of equity awards covering a total of 2,750,000 shares of the
Company’s common stock, no more than 300,000 shares of which may be restricted stock or restricted stock units. A restricted stock unit is a notional
account representing the right to receive a share of Ordinary Common Stock (or, at the Company’s option, cash in lieu thereof) at some future date. Under the
2006 MIP, the exercisability of certain options and the vesting of certain restricted stock units is subject to certain performance targets. The Director Plan
covers 120,000 shares of the Company’s common stock, no more than 15,000 of which may be restricted stock or restricted stock units, and provides for the
issuance of options and restricted stock or restricted stock units to directors immediately following each annual meeting of shareholders in 2006 and 2007.
The ESPP covers 100,000 shares of the Company’s common stock and permits employees of the Company to purchase Common Stock at a 5 percent
discount. The initial period of activity for the ESPP will be August 1, 2006 through December 31, 2006.

Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS 123 (revised 2004) “Share-Based Payment”
(“SFAS 123R”), using the modified prospective transition method and therefore has not restated results for prior periods. Under this transition method, stock-
based compensation expense for the three months and six months ended June 30, 2006 includes compensation expense for all stock-based compensation
awards granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of
SFAS No. 123. Stock-based compensation expense for all stock-based compensation awards granted after January 1, 2006 is based on the grant date fair value
estimated in accordance with the provisions of SFAS 123R. The Company recognizes these compensation costs on a straight-line basis over the requisite
service period, which is generally the option vesting term ranging from three to four years. Prior to the adoption of SFAS 123R, the Company recorded stock-
based compensation under Accounting Principles Board (“APB”) Opinion No. 25, “Accounting for Stock Issued to Employees” (“APB 25”).

The Company uses the Black-Scholes-Merton formula to estimate the fair value of stock options granted to employees and recorded stock compensation
expense of $6.6 million and $12.1 million for the three months and six months ended June 30, 2006, respectively. As stock-based compensation expense
recognized in the condensed consolidated statements of income for the three months and six months ended June 30, 2006 is based on awards ultimately
expected to vest, it has been reduced for estimated forfeitures, currently estimated at four percent, as required by SFAS 123R. In the Company’s pro forma
information that was required under SFAS 123 for the periods prior to January 1, 2006, the Company accounted for its forfeitures as they occurred. The
impact of adopting SFAS 123R to the condensed consolidated financial statements for the three months and six months ended June 30, 2006 was a reduction
to net income of $1.3 million and $2.5 million, respectively, or a decrease of $0.04 and $0.07, respectively, on basic income per common share and a
decrease of $0.03 and $0.06, respectively, on fully-diluted income per common share.

SFAS 123R also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as
an operating cash flow. In the three months and six ended June 30, 2006, the tax deductions related to stock compensation were not recognized because of
the availability of NOLs, and thus there were no such financing cash flows reported.
For the six months ended June 30, 2006, the weighted average grant date fair value of the stock options granted was $14.17 as estimated using the Black-Scholes-Merton option-pricing model based on the following weighted average assumptions:

<table>
<thead>
<tr>
<th>Risk-free interest rate</th>
<th>4.82%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expected life</td>
<td>4 years</td>
</tr>
<tr>
<td>Expected volatility</td>
<td>29.90%</td>
</tr>
<tr>
<td>Expected dividend yield</td>
<td>0.00%</td>
</tr>
</tbody>
</table>

As part of its SFAS 123R adoption, management determined that volatility based on actively traded equities of companies that are similar to the Company is a better indicator of expected volatility and future stock price trends than historical volatility, due to the lack of sufficient history of the Company subsequent to the Company’s emergence from bankruptcy on the Effective Date.

Summarized information related to the Company’s stock options for the six months ended June 30, 2006 is as follows:

<table>
<thead>
<tr>
<th></th>
<th>Options</th>
<th>Weighted Average Exercise Price</th>
<th>Weighted Average Remaining Contractual Term (in years)</th>
<th>Aggregate Intrinsic Value (in thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Outstanding, beginning of period</td>
<td>4,014,711</td>
<td>$18.50</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Granted</td>
<td>1,451,553</td>
<td>36.05</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cancelled</td>
<td>(195,202)</td>
<td>24.74</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Exercised</td>
<td>(415,049)</td>
<td>18.68</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Outstanding, end of period</td>
<td>4,856,013</td>
<td>$23.48</td>
<td>5.79</td>
<td>$106,628</td>
</tr>
<tr>
<td>Vested and expected to vest at end of period</td>
<td>4,646,763</td>
<td>$23.27</td>
<td>1.07</td>
<td>$103,031</td>
</tr>
<tr>
<td>Exercisable, end of period</td>
<td>259,163</td>
<td>$28.32</td>
<td>7.35</td>
<td>$ 4,436</td>
</tr>
</tbody>
</table>

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (based upon the difference between the Company’s closing stock price on the last trading day of the fiscal 2006 second quarter of $45.31 and the exercise price) for all in-the-money options as of June 30, 2006. This amount changes based on the fair market value of the Company’s stock. The total pre-tax intrinsic value of options exercised (based on the difference between the Company’s closing stock price on the day the option was exercised and the exercise price) during the six months ended June 30, 2006 was $7.9 million.

As of June 30, 2006, there was $37.7 million of total unrecognized compensation expense related to nonvested stock options that is expected to be recognized over a weighted average remaining recognition period of 1.69 years. The total fair value of shares vested during the three months and six months ended June 30, 2006 was $0.1 million and $9.4 million, respectively.

During the six months ended June 30, 2006, the Company granted 956,002 options to members of management at a weighted average grant date fair value of approximately $13.35 and at an exercise price of $38.52, which was equal to the price of the Company’s stock on February 24, 2006, the date that the option grants were approved by the board of directors of the Company.

The Company granted an additional 199,463 options pursuant to the January 31, 2006 acquisition of NIA (see Note B below), including 99,463 Incentive Stock Options (“ISOs”). The weighted average grant date fair value of the 100,000 options, other than ISOs, granted to NIA employees was approximately $11.01. The 99,463 ISOs were granted to three employees previously employed by NIA in exchange for outstanding NIA incentive stock options held by such individuals and were granted at exercise prices that ranged from $4.44 to $7.66 per share, which prices were determined based on the exercise price of the NIA options exchanged times the exchange ratio equal to the price of the Company’s stock at closing to the
purchase price per share of NIA paid by the Company in the acquisition. The options had a weighted average grant date fair value of approximately $32.24. Stock-based compensation expense related to the ISOs for the three months and six months ended June 30, 2006 was approximately $0.3 million and $0.4 million, respectively. The remaining 296,088 options granted to management in the six months ended June 30, 2006 were granted at exercise prices which equaled the fair market value of the Company’s Ordinary Common Stock on the respective grant dates, which included options to purchase 209,388 shares granted upon exercise of 2004 Options (defined below) pursuant to the amendments as described below.

All of the Company’s options granted during the six months ended June 30, 2006 vest ratably on each anniversary date over the three years subsequent to grant, and all have a ten year life.

Restricted Stock Awards

During the year ended December 31, 2005, the Company granted 140,636 shares of restricted stock pursuant to the 2003 MIP, 14,507 of which were vested and 126,129 of which vest ratably on each anniversary date over the four years subsequent to grant. Of these grants, 10,872 shares were cancelled pursuant to terminations of employment, resulting in a total of 115,257 outstanding unvested shares of restricted stock at December 31, 2005.

Summarized information related to the Company’s nonvested restricted stock awards for the six months ended June 30, 2006 is as follows:

<table>
<thead>
<tr>
<th>Shares</th>
<th>Weighted Average Grant Date Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Outstanding, beginning of period</td>
<td>115,257</td>
</tr>
<tr>
<td>Awarded</td>
<td>6,750</td>
</tr>
<tr>
<td>Vested</td>
<td>(25,243)</td>
</tr>
<tr>
<td>Forfeited</td>
<td>(8,243)</td>
</tr>
<tr>
<td>Outstanding, ending of period</td>
<td>88,521</td>
</tr>
</tbody>
</table>

The 6,750 restricted stock awards granted in the six months ended June 30, 2006 vest ratably on each anniversary date over the three years subsequent to grant. As of June 30, 2006, there was $2.6 million of unrecognized stock-based compensation expense related to nonvested restricted stock awards. This cost is expected to be recognized over a weighted-average period of 2.69 years.

Restricted Stock Units

During the six months ended June 30, 2006, the Company granted 116,327 restricted stock units pursuant to the 2006 MIP which vest ratably on each anniversary date over the three years subsequent to grant. As of June 30, 2006, there was $4.4 million of unrecognized stock-based compensation expense related to nonvested restricted stock units. This cost is expected to be recognized over a weighted-average period of 2.65 years.

Common Stock Warrants

On the Effective Date, Magellan and 88 of its subsidiaries consummated their Third Joint Amended Plan of Reorganization, as modified and confirmed (the “Plan”). Under the Plan, the Company issued 570,825 warrants to purchase common stock of the Company at a purchase price of $30.46 per share at anytime until January 5, 2011. As of June 30, 2006, 570,384 of these warrants remain outstanding. Also on the Effective Date and pursuant to the Plan, the Company entered into a warrant agreement with Aetna whereby Aetna had the option to purchase, between January 1, 2006 and January 5, 2009, 230,000 shares of Ordinary Common Stock at a purchase price of $10.48 per share. On January 30, 2006, Aetna effected a cashless exercise for all of their warrants, which resulted in 150,815 shares being issued to Aetna.
Option Modification

On January 3, 2006, the Company amended certain stock options outstanding under the 2003 MIP. The amendments, as further described below, were intended primarily to bring the features of such options into compliance with certain requirements established by Section 409A of the Internal Revenue Code of 1986, as amended (the “Code”), which was added to the Code by the American Jobs Creation Act of 2004 and governs as a general matter the federal income tax treatment of deferred compensation. The amended options were originally issued in connection with the consummation of the Plan, which occurred on the Effective Date (the “2004 Options”). Because the exercise price of such 2004 Options may be considered to have been less than the fair market value of the shares that may be acquired upon exercise of such options as determined by the market trading in such shares following the consummation of the Plan, such options might be subject to the provisions of Section 409A, including certain penalty tax provisions on the option holders.

The amendments in each case reduced the period in which the 2004 Options, once vested, could be exercised from the tenth anniversary of the date of grant to the end of the calendar year in which each option first becomes exercisable. The vesting schedule of the options was not changed and no change was made in the exercise price or other material terms.

In addition, the 2004 Options issued to the Company’s Chief Executive Officer, Chief Operating Officer and Chief Financial Officer (the “Senior Executives”) were also amended to defer until January 5, 2007 the exercisability of all but 137,398 of their options that vest in January 2006. This deferral was agreed upon in connection with the waiver by the Company of the restriction on sale before January 5, 2007 of 413,003 shares held by the Senior Executives, that they had previously acquired upon exercise of a portion of their 2004 Options that vested in January 2005.

In connection with these amendments, the Company agreed to grant new options to option holders, other than the Senior Executives, upon exercise of their 2004 Options. The new options will be in an amount equal to the number of options exercised, will have exercise prices equal to the market price on the date of grant and will vest ratably on each anniversary date over the three years subsequent to grant. Of the remaining 816,848 shares available for future grants under the terms of the 2003 MIP as of June 30, 2006, 682,403 shares are reserved for future issuances of such options, which issuances would occur in 2006, 2007 and 2008 as the 2004 Options vest and are exercised. In the six months ended June 30, 2006, options to purchase 209,388 shares were granted pursuant to these amendments upon exercise of 2004 Options during this period.

Recent Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board (“FASB”) issued FASB Interpretation (“FIN”) No. 48, “Accounting for Uncertainty in Income Taxes—An Interpretation of FASB Statement No. 109” (“FIN 48”), which prescribes a minimum recognition threshold and measurement methodology for tax positions taken or expected to be taken in a tax return. FIN 48 will be effective beginning January 1, 2007. The Company has not yet evaluated the impact of implementation of FIN 48 on its consolidated financial statements.

Reclassifications

Certain amounts previously reported for the three months and six months ended June 30, 2005 have been reclassified to conform to the presentation of amounts reported for the three months and six months ended June 30, 2006.
NOTE B—Acquisitions

Acquisition of National Imaging Associates

On January 31, 2006, the Company acquired all of the outstanding stock of NIA, a privately held radiology benefits management ("RBM") firm headquartered in Hackensack, New Jersey, for approximately $121 million in cash, after giving effect to cash acquired in the transaction, and NIA became a wholly owned subsidiary of Magellan.

NIA manages diagnostic imaging services on a non-risk basis for its health plans to ensure that such services are clinically appropriate and cost effective. NIA has approximately 17.9 million covered lives under contract as of June 30, 2006. The Company reports the results of operations of NIA as a separate segment entitled Magellan Radiology Benefits Management ("Radiology Benefits Management"). See Note F—Business Segment Information.

The estimated fair values of NIA assets acquired and liabilities assumed at the date of the acquisition are summarized as follows (in thousands):

<table>
<thead>
<tr>
<th>Assets acquired:</th>
<th>$135,419</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current assets</td>
<td>$10,137</td>
</tr>
<tr>
<td>Property and equipment, net</td>
<td>6,018</td>
</tr>
<tr>
<td>Other assets</td>
<td>85</td>
</tr>
<tr>
<td>Goodwill</td>
<td>105,649</td>
</tr>
<tr>
<td>Other identified intangible assets</td>
<td>13,530</td>
</tr>
<tr>
<td><strong>Total assets acquired</strong></td>
<td><strong>135,419</strong></td>
</tr>
<tr>
<td>Liabilities assumed:</td>
<td>$5,689</td>
</tr>
<tr>
<td>Current liabilities</td>
<td>5,201</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>488</td>
</tr>
<tr>
<td><strong>Total liabilities assumed</strong></td>
<td><strong>5,689</strong></td>
</tr>
<tr>
<td>Net assets acquired</td>
<td>$129,730</td>
</tr>
</tbody>
</table>

The purchase price has been allocated based upon the estimated fair value of net assets acquired at the date of acquisition. A portion of the excess purchase price over tangible net assets acquired has been allocated to identified intangible assets totaling $13.5 million, consisting of customer contracts in the amount of $12.6 million, which is being amortized over 10 years, and developed software in the amount of $0.9 million, which is being amortized over 5 years. In addition, the excess of purchase price over tangible net assets and identified intangible assets acquired resulted in $105.6 million of non-tax deductible goodwill.
As a result of the acquisition of NIA, the Company approved an exit plan for certain NIA operations and activities. The Company’s plan to exit certain facilities of NIA resulted in assumed liabilities of $0.7 million to terminate an initial estimate of 28 employees and $0.4 million to close excess facilities, which were recorded based on EITF No. 95-3, “Recognition of Liabilities in Connection with a Purchase Business Combination.” Such assumed liabilities are reflected in “Accrued liabilities” in the condensed consolidated financial statements. Additional liabilities may be recognized in future periods as the Company completes its analysis of this acquisition. A rollforward of exit plan liabilities assumed is as follows (in thousands):

<table>
<thead>
<tr>
<th>Balance</th>
<th>Additions</th>
<th>Payments</th>
<th>Adjustments (1)</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>January 31, 2006</td>
<td></td>
<td></td>
<td></td>
<td>June 30, 2006</td>
</tr>
<tr>
<td>Employee severance and termination benefits</td>
<td>$684</td>
<td>$(189)</td>
<td>$(41)</td>
<td>$454</td>
</tr>
<tr>
<td>Lease termination and other costs</td>
<td>$392</td>
<td></td>
<td></td>
<td>$371</td>
</tr>
<tr>
<td></td>
<td>$1,076</td>
<td></td>
<td></td>
<td>$825</td>
</tr>
</tbody>
</table>

(1) The estimated costs of employee severance and termination was adjusted to reflect the net retention of three employees, therefore reducing the number of employees receiving termination benefits to 25.

The results of NIA have been included in the Company’s consolidated financial statements since January 31, 2006, the date of acquisition. Had NIA’s results of operations been included in the Company’s results of operations since January 1, 2006, there would have been no material effect on the Company’s consolidated results of operations. The following unaudited supplemental pro forma information represents the Company’s consolidated results of operations as if the acquisition of NIA had occurred on January 1, 2005 and after giving effect to certain adjustments including interest income, depreciation and amortization, and stock-based compensation. Such pro forma information does not purport to be indicative of operating results that would have been reported had the acquisition of NIA occurred on January 1, 2005 (in thousands):

<table>
<thead>
<tr>
<th>Pro Forma (unaudited)</th>
<th>Three months ended June 30, 2005</th>
<th>Six months ended June 30, 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net revenue</td>
<td>$474,713</td>
<td>$937,385</td>
</tr>
<tr>
<td>Net income</td>
<td>20,501</td>
<td>42,635</td>
</tr>
<tr>
<td>Income per common share available to common stockholders — basic:</td>
<td>$0.58</td>
<td>$1.20</td>
</tr>
<tr>
<td>Income per common share available to common stockholders — diluted:</td>
<td>$0.55</td>
<td>$1.16</td>
</tr>
</tbody>
</table>

Acquisition of ICORE Healthcare, LLC

On June 28, 2006, the Company entered into a definitive agreement to acquire all of the outstanding ownership interests of ICORE Healthcare LLC, (“ICORE”) a privately held specialty pharmaceutical management firm headquartered in Orlando, Florida. Under the terms of the definitive agreement, the Company will pay a base price of approximately $210 million, before giving effect to cash acquired in the transaction, and may be required to pay a potential earn-out of up to $75 million to the owners of ICORE, all of whom are members of ICORE’s management team. The base price is payable in cash of approximately $186 million and, through a reinvestment, in restricted stock of approximately $24 million, which restricted stock will vest fifty percent each on the second and third anniversaries of the date of grant.
provided the individuals do not terminate their employment prior to each such anniversary. The portion of the base price paid in restricted stock will be treated as compensation expense and not as purchase price. Of the cash portion of the purchase price, $25 million will be held back by the Company for three years to cover any indemnity claims under the definitive agreement, and the remaining $161 million, as well as transaction and other related costs, will be paid at closing. The earn-out will be comprised of two parts; up to $25 million based on earnings targets, as defined, for the 18-month period ending December 31, 2007 and up to $50 million based on earnings targets, as defined, in 2008. The earn-out, if earned, is payable 33 percent in cash and 67 percent in restricted stock that will vest over two years after issuance. The earn-out will be paid to the five executives of ICORE, who will become employees of the Company. Upon achieving the targets, the earn-out will only be paid if the individuals remain employees in good standing with the Company. As a result of this requirement, the earn-out payments will be treated as compensation expense and not as additional purchase price.

ICORE works with health plans to manage specialty drugs used in the treatment of cancer, multiple sclerosis, hemophilia, infertility, rheumatoid arthritis, chronic forms of hepatitis and other diseases. ICORE holds contracts with approximately 36 health plans with approximately 60 million covered lives under contract in commercial, Medicare and Medicaid programs at June 30, 2006. The Company will report the results of operations of ICORE as a separate segment entitled Specialty Pharmaceutical Management. All material closing conditions for the transaction involving third parties have been met, and the Company expects that the transaction will be consummated on July 31, 2006.

NOTE C—Long Term Debt and Capital Lease Obligations

Information with regard to the Company’s long-term debt and capital lease obligations at December 31, 2005 and June 30, 2006 is as follows (in thousands):

<table>
<thead>
<tr>
<th>Credit Agreement:</th>
<th>December 31, 2005</th>
<th>June 30, 2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revolving Loan Facility due through 2008</td>
<td>$—</td>
<td>$—</td>
</tr>
<tr>
<td>Term Loan Facility (7.32% to 7.42% at June 30, 2006) due through 2008</td>
<td>62,500</td>
<td>50,000</td>
</tr>
<tr>
<td>4.36% to 6.00% capital lease obligations due through 2008</td>
<td>584</td>
<td>427</td>
</tr>
<tr>
<td></td>
<td>63,084</td>
<td>50,427</td>
</tr>
<tr>
<td>Less current maturities of long-term debt and capital lease obligations</td>
<td>(25,194)</td>
<td>(25,196)</td>
</tr>
<tr>
<td></td>
<td>$37,890</td>
<td>$25,231</td>
</tr>
</tbody>
</table>
NOTE D—Income per Common Share

The following tables reconcile income (numerator) and shares (denominator) used in the computations of income from continuing operations per common share (in thousands, except per share data):

| | Three Months Ended June 30 | | Six Months Ended June 30 | |
| | 2005 (restated) | 2006 | 2005 (restated) | 2006 |
| Numerator: | | | | |
| Income from continuing operations—basic and diluted | $20,901 | $20,224 | $43,981 | $42,539 |
| Denominator: | | | | |
| Weighted average number of common shares outstanding—basic | | | | |
| Common stock equivalents—stock options | 35,567 | 36,999 | 35,475 | 36,852 |
| Common stock equivalents—warrants | 1,208 | 1,440 | 1,210 | 1,407 |
| Common stock equivalents—restricted stock | 205 | 146 | 213 | 123 |
| Common stock equivalents—restricted stock units | | | | |
| Weighted average number of common shares outstanding—diluted | 35,762 | 37,445 | 35,688 | 37,055 |
| Income from continuing operations per common share—basic | | | | |
| Income from continuing operations per common share—diluted | | | | |

The weighted average number of common shares outstanding for the three months and six months ended June 30, 2005 and 2006 was calculated using outstanding shares of the Company’s Ordinary Common Stock and Multi-Vote Common Stock. Common stock equivalents included in the calculation of diluted weighted average common shares outstanding for the three months and six months ended June 30, 2005 and 2006 represent stock options to purchase shares of the Company’s Ordinary Common Stock, restricted stock awards and restricted stock units, and shares of Ordinary Common Stock related to certain warrants issued on the Effective Date.

NOTE E—Commitments and Contingencies

Insurance

The Company maintains a program of insurance coverage for a broad range of risks in its business. As part of this program of insurance, the Company is self-insured for a portion of its general, professional and managed care liability risks.

The Company has renewed its general, professional and managed care liability insurance policies with unaffiliated insurers for a one-year period from June 17, 2006 to June 17, 2007. The general liability policies are written on an “occurrence” basis, subject to a $0.1 million per claim un-aggregated self-insured retention. The professional liability and managed care errors and omissions liability policies are written on a “claims-made” basis, subject to a $1.0 million per claim ($10.0 million per class action claim) un-aggregated self-insured retention for managed care liability, and a $0.1 million per claim un-aggregated self-insured retention for professional liability. The Company is responsible for claims within its self-insured retentions, including portions of claims reported after the expiration date of the policies if they are not renewed, or if policy limits are exceeded. The Company also purchases excess liability coverage in an amount that management believes to be reasonable for the size and profile of the organization.

21
Legal

The Company is subject to or party to certain litigation and claims relating to its operations and business practices. Except as otherwise provided under the Plan, litigation asserting claims against the Company and its subsidiaries that were parties to the chapter 11 proceedings for pre-petition obligations (the “Pre-petition Litigation”) was enjoined as of the Effective Date as a consequence of the confirmation of the Plan and may not be pursued over the objection of Magellan or such subsidiary unless relief is provided from the effect of the injunction. The Company believes that the Pre-petition Litigation claims with respect to which distributions have been provided for under the Plan constitute general unsecured claims and, to the extent allowed by the Plan, would be resolved as other general unsecured creditor claims.

In the opinion of management, the Company has recorded reserves that are adequate to cover litigation, claims or assessments that have been or may be asserted against the Company, and for which the outcome is probable and reasonably estimable. Management believes that the resolution of all known litigation and claims will not have a material adverse effect on the Company’s financial position or results of operations; however, there can be no assurance in that regard.

Operating Leases

The Company leases certain of its operating facilities. The leases, which expire at various dates through January 2013, generally require the Company to pay all maintenance, property tax and insurance costs.

NOTE F—Business Segment Information

The Company is engaged in the specialty healthcare management services business. It currently provides managed behavioral healthcare services, and radiology benefits management, and will provide specialty pharmaceutical management as a result of its pending acquisition of ICORE.

The Company provides services to health plans, insurance companies, corporations, labor unions and various governmental agencies. The Company’s business is divided into the following five segments, based on the services it provides and/or the customers that it serves, as described below.

Managed Behavioral Healthcare. The Company’s Managed Behavioral Healthcare business is composed of three of the Company’s segments, each as described further below. This line of business generally reflects the Company’s coordination and management of the delivery of behavioral healthcare treatment services that are provided through its contracted network of third-party treatment providers, which includes psychiatrists, psychologists, other behavioral health professionals, psychiatric hospitals, general medical facilities with psychiatric beds, residential treatment centers and other treatment facilities. The treatment services provided through the Company’s provider network include outpatient programs (such as counseling or therapy), intermediate care programs (such as intensive outpatient programs and partial hospitalization services), inpatient treatment and crisis intervention services. The Company, however, generally does not directly provide, or own any provider of, treatment services. The Managed Behavioral Healthcare business is managed based on the services provided and/or the customers served, through the following three segments:

Health Plan. The Managed Behavioral Healthcare Health Plan segment (“Health Plan”) generally reflects managed behavioral healthcare services provided under contracts with managed care companies, health insurers and other health plans. Health Plan’s contracts encompass both risk-based and administrative services only (“ASO”) contracts for commercial, Medicaid and Medicare members of the health plan. Although certain health plans provide their own managed behavioral healthcare services, many health plans “carve out” behavioral healthcare from their general
healthcare services and subcontract such services to managed behavioral healthcare companies such as the Company. In Health Plan, the Company’s members are the beneficiaries of the health plan (the employees and dependents of the customer of the health plan), for which the behavioral healthcare services have been carved out to the Company.

**Employer.** The Managed Behavioral Healthcare Employer segment (“Employer”) generally reflects the provision of employee assistance program (“EAP”) services, managed behavioral healthcare services and integrated products under contracts with employers, including corporations and governmental agencies, and labor unions. Employer managed behavioral healthcare services are primarily ASO products.

**Public Sector.** The Managed Behavioral Healthcare Public Sector segment (“Public Sector”) generally reflects managed behavioral healthcare services provided to Medicaid recipients under contracts with state and local governmental agencies. Public Sector contracts encompass both risk-based and ASO contracts.

**Radiology Benefits Management.** The Company’s Radiology Benefits Management segment generally reflects the management of diagnostic imaging services on a non-risk basis for health plans to ensure that such services are clinically appropriate and cost effective.

**Corporate and Other.** This segment of the Company is comprised primarily of operational support functions such as sales and marketing and information technology, as well as corporate support functions such as executive, finance, human resources and legal.

The accounting policies of these segments are the same as those described in Note A—“General—Summary of Significant Accounting Policies.” The Company evaluates performance of its segments based on profit or loss from continuing operations before depreciation and amortization, interest expense, interest income, stock compensation expense, gain on sale of assets, income taxes and minority interest (“Segment Profit”). Management uses Segment Profit information for internal reporting and control purposes and considers it important in making decisions regarding the allocation of capital and other resources, risk assessment and employee compensation, among other matters. Intersegment sales and transfers are not significant. The following tables summarize, for the periods indicated, operating results by business segment (in thousands):

<table>
<thead>
<tr>
<th>Three Months Ended June 30, 2005</th>
<th>Health Plan</th>
<th>Employer</th>
<th>Public Sector</th>
<th>Corporate and Other</th>
<th>Consolidated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net revenue</td>
<td>$233,494</td>
<td>$31,741</td>
<td>$199,309</td>
<td>—</td>
<td>$464,544</td>
</tr>
<tr>
<td>Cost of care</td>
<td>132,142</td>
<td>7,786</td>
<td>176,993</td>
<td>—</td>
<td>316,921</td>
</tr>
<tr>
<td>Direct service costs</td>
<td>42,296</td>
<td>16,430</td>
<td>7,614</td>
<td>—</td>
<td>66,340</td>
</tr>
<tr>
<td>Other operating expenses</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>23,861</td>
<td>23,861</td>
</tr>
<tr>
<td>Equity in earnings of unconsolidated subsidiaries</td>
<td>(1,503)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>(1,503)</td>
</tr>
<tr>
<td>Segment profit (loss)</td>
<td>$60,559</td>
<td>$7,525</td>
<td>$14,702</td>
<td>$(23,861)</td>
<td>$58,925</td>
</tr>
</tbody>
</table>

23
<table>
<thead>
<tr>
<th>Three Months Ended June 30, 2006</th>
<th>Health Plan</th>
<th>Employer</th>
<th>Public Sector</th>
<th>Radiology Benefits Management</th>
<th>Corporate and Other</th>
<th>Consolidated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net revenue</td>
<td>$159,381</td>
<td>$32,057</td>
<td>$195,066</td>
<td>$12,429</td>
<td>$398,933</td>
<td></td>
</tr>
<tr>
<td>Cost of care</td>
<td>89,899</td>
<td>6,911</td>
<td>165,896</td>
<td>89,899</td>
<td>32,057</td>
<td>262,706</td>
</tr>
<tr>
<td>Direct service costs</td>
<td>25,516</td>
<td>17,427</td>
<td>8,918</td>
<td>10,130</td>
<td>61,991</td>
<td></td>
</tr>
<tr>
<td>Other operating expenses</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>24,113</td>
<td>24,113</td>
<td></td>
</tr>
<tr>
<td>Segment profit (loss)</td>
<td>$ 43,966</td>
<td>$ 7,719</td>
<td>$ 20,252</td>
<td>$ 2,299</td>
<td>$(24,113)</td>
<td>$ 50,123</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Six Months Ended June 30, 2005</th>
<th>Health Plan</th>
<th>Employer</th>
<th>Public Sector</th>
<th>Radiology Benefits Management</th>
<th>Corporate and Other</th>
<th>Consolidated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net revenue</td>
<td>$458,396</td>
<td>$63,401</td>
<td>$395,501</td>
<td>—</td>
<td>$917,298</td>
<td></td>
</tr>
<tr>
<td>Cost of care</td>
<td>253,870</td>
<td>15,646</td>
<td>351,613</td>
<td>253,870</td>
<td>15,646</td>
<td>521,129</td>
</tr>
<tr>
<td>Direct service costs</td>
<td>81,878</td>
<td>32,135</td>
<td>15,201</td>
<td>81,878</td>
<td>32,135</td>
<td>129,214</td>
</tr>
<tr>
<td>Other operating expenses</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>49,708</td>
<td>49,708</td>
<td></td>
</tr>
<tr>
<td>Equity in earnings of unconsolidated subsidiaries</td>
<td>(2,952)</td>
<td>—</td>
<td>—</td>
<td>(2,952)</td>
<td>(2,952)</td>
<td></td>
</tr>
<tr>
<td>Segment profit (loss)</td>
<td>$125,600</td>
<td>$15,620</td>
<td>$28,687</td>
<td>$28,687</td>
<td>$(49,708)</td>
<td>$120,199</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Six Months Ended June 30, 2006</th>
<th>Health Plan</th>
<th>Employer</th>
<th>Public Sector</th>
<th>Radiology Benefits Management</th>
<th>Corporate and Other</th>
<th>Consolidated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net revenue</td>
<td>$317,168</td>
<td>$65,237</td>
<td>$396,965</td>
<td>$20,159</td>
<td>$799,529</td>
<td></td>
</tr>
<tr>
<td>Cost of care</td>
<td>176,175</td>
<td>15,066</td>
<td>341,300</td>
<td>176,175</td>
<td>15,066</td>
<td>331,241</td>
</tr>
<tr>
<td>Direct service costs</td>
<td>51,849</td>
<td>34,122</td>
<td>16,980</td>
<td>51,849</td>
<td>34,122</td>
<td>86,061</td>
</tr>
<tr>
<td>Other operating expenses</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>48,740</td>
<td>48,740</td>
<td></td>
</tr>
<tr>
<td>Equity in earnings of unconsolidated subsidiaries</td>
<td>(390)</td>
<td>—</td>
<td>—</td>
<td>(390)</td>
<td>(390)</td>
<td></td>
</tr>
<tr>
<td>Segment profit (loss)</td>
<td>$ 89,534</td>
<td>$16,049</td>
<td>$38,685</td>
<td>$38,685</td>
<td>$(48,740)</td>
<td>$99,306</td>
</tr>
</tbody>
</table>

The following table reconciles Segment Profit to consolidated income from continuing operations before income taxes and minority interest (in thousands):

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Segment Profit</td>
<td>$ 58,925 $ 50,123</td>
<td>$120,199 $ 99,306</td>
</tr>
<tr>
<td>Depreciation and amortization</td>
<td>(13,573) $ (11,333)</td>
<td>(24,791) $ (21,990)</td>
</tr>
<tr>
<td>Interest expense</td>
<td>(8,611) $ (1,721)</td>
<td>(17,250) $ (3,690)</td>
</tr>
<tr>
<td>Interest income</td>
<td>3,899 $ 4,921</td>
<td>6,932 $ 9,138</td>
</tr>
<tr>
<td>Stock compensation expense</td>
<td>(4,419) $ (6,594)</td>
<td>(8,169) $ (12,094)</td>
</tr>
<tr>
<td>Gain on sale of assets</td>
<td>—</td>
<td>403 $ 5,148</td>
</tr>
<tr>
<td>Income from continuing operations before income taxes and minority interest</td>
<td>$ 36,221 $ 35,799</td>
<td>$ 76,921 $ 75,818</td>
</tr>
</tbody>
</table>
Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis of the financial condition and results of operations of Magellan Health Services, Inc. (“Magellan”), and its majority-owned subsidiaries and all variable interest entities (“VIEs”) for which Magellan is the primary beneficiary (together with Magellan, the “Company”) should be read together with the Condensed Consolidated Financial Statements and the notes to the Condensed Consolidated Financial Statements included elsewhere in this Quarterly Report on Form 10-Q and the Company’s Annual Report on Form 10-K for the year ended December 31, 2005, which was filed with the Securities and Exchange Commission (“SEC”) on March 8, 2006.

Forward-Looking Statements

This Form 10-Q includes “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”) and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Although the Company believes that its plans, intentions and expectations as reflected in such forward-looking statements are reasonable, it can give no assurance that such plans, intentions or expectations will be achieved. Prospective investors are cautioned that any such forward-looking statements are not guarantees of future performance and involve risks and uncertainties, and that actual results may differ materially from those contemplated by such forward-looking statements. Important factors currently known to management that could cause actual results to differ materially from those in forward-looking statements include:

- the Company’s inability to renegotiate or extend expiring customer contracts, or the termination of customer contracts;
- the Company’s inability to integrate acquisitions, including National Imaging Associates and ICORE Healthcare LLC (each as discussed below), in a timely and effective manner;
- changes in business practices of the industry, including the possibility that certain of the Company’s managed care customers could seek to provide managed healthcare services directly to their subscribers, instead of contracting with the Company for such services;
- the impact of changes in the contracting model for Medicaid contracts, including certain changes in the contracting model used by states for managed healthcare services contracts relating to Medicaid lives;
- the impact of healthcare costs on fixed fee contracts;
- the Company’s dependence on government spending for managed healthcare, including changes in federal, state and local healthcare policies;
- restricted covenants in the Company’s debt instruments;
- present or future state regulations and contractual requirements that the Company provide financial assurance of its ability to meet its obligations;
- the impact of the competitive environment in the managed healthcare services industry may limit the Company’s ability to maintain or obtain contracts, as well as to its ability to maintain or increase its rates;
- the possible impact of healthcare reform;
- government regulation;
- the inability to realize the value of goodwill and intangible assets;
future changes in the composition of the Company’s stockholder population which could, in certain circumstances, limit the ability of the Company to utilize its Net Operating Losses (“NOLs”);

pending or future actions or claims for professional liability;

claims brought against the Company that either exceed the scope of the Company’s liability coverage or result in denial of coverage;

class action suits and other legal proceedings; and

the impact of governmental investigations.

Further discussion of factors currently known to management that could cause actual results to differ materially from those in forward-looking statements is set forth under the heading “Risk Factors” in Item 1A of Magellan’s Annual Report on Form 10-K for the year ended December 31, 2005. When used in this Quarterly Report on Form 10-Q, the words “estimate,” “anticipate,” “expect,” “believe,” “should,” and similar expressions are intended to be forward-looking statements. Magellan undertakes no obligation to update or revise forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes to future operating results over time.

Overview

The Company is engaged in the specialty healthcare management services business. Through fiscal 2005, the Company predominantly operated in the managed behavioral healthcare business. During fiscal 2006, the Company has expanded into radiology benefits management as a result of its acquisition of National Imaging Associates, Inc. (“NIA”), as discussed further below. Also, the Company’s planned acquisition of ICORE Healthcare, LLC (“ICORE”) will result in its entry into specialty pharmaceutical management, as discussed further below.

Managed Behavioral Healthcare

The Company, directly and through its subsidiaries, coordinates and manages the delivery of behavioral healthcare treatment services that are provided through its contracted network of third-party treatment providers, which includes psychiatrists, psychologists, other behavioral health professionals, psychiatric hospitals, general medical facilities with psychiatric beds, residential treatment centers and other treatment facilities. The treatment services provided through the Company’s provider network include outpatient programs (such as counseling or therapy), intermediate care programs (such as intensive outpatient programs and partial hospitalization services), inpatient treatment and crisis intervention services. The Company, however, generally does not directly provide, or own any provider of, treatment services. The Company provides its management services primarily through: (i) risk-based products, where the Company assumes all or a portion of the responsibility for the cost of providing treatment services in exchange for a fixed per member per month fee, (ii) administrative services only (“ASO”) products, where the Company provides services such as utilization review, claims administration and/or provider network management but does not assume responsibility for the cost of the treatment services, (iii) employee assistance programs (“EAPs”) where the Company provides short-term outpatient counseling and (iv) products that combine features of some or all of the Company’s risk-based, ASO or EAP products. At June 30, 2006, the Company managed the behavioral healthcare of approximately 42.5 million individuals.
The following table sets forth the approximate number of managed behavioral healthcare covered lives as of June 30, 2005 and 2006. The table also shows revenue for the three months and six months ended June 30, 2005 and 2006, for the types of managed behavioral healthcare programs offered by the Company:

Programs

<table>
<thead>
<tr>
<th>Programs</th>
<th>Covered Lives</th>
<th>Percent</th>
<th>Revenue (in millions)</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Three Months Ended June 30, 2005</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Risk-Based products</td>
<td>14.2</td>
<td>24.3%</td>
<td>$385.4</td>
<td>83.0%</td>
</tr>
<tr>
<td>EAP products</td>
<td>13.3</td>
<td>22.8%</td>
<td>27.9</td>
<td>6.0%</td>
</tr>
<tr>
<td>ASO products</td>
<td>30.9</td>
<td>52.9%</td>
<td>51.2</td>
<td>11.0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>58.4</strong></td>
<td><strong>100.0%</strong></td>
<td><strong>$464.5</strong></td>
<td><strong>100.0%</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Programs</th>
<th>Covered Lives</th>
<th>Percent</th>
<th>Revenue (in millions)</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Three Months Ended June 30, 2006</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Risk-Based products</td>
<td>9.1</td>
<td>21.4%</td>
<td>$332.0</td>
<td>83.6%</td>
</tr>
<tr>
<td>EAP products</td>
<td>13.6</td>
<td>32.0%</td>
<td>26.9</td>
<td>6.9%</td>
</tr>
<tr>
<td>ASO products</td>
<td>19.8</td>
<td>46.6%</td>
<td>36.6</td>
<td>9.5%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>42.5</strong></td>
<td><strong>100.0%</strong></td>
<td><strong>$386.5</strong></td>
<td><strong>100.0%</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Programs</th>
<th>Covered Lives</th>
<th>Percent</th>
<th>Revenue (in millions)</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Six Months Ended June 30, 2005</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Risk-Based products</td>
<td>14.2</td>
<td>24.3%</td>
<td>$760.2</td>
<td>82.9%</td>
</tr>
<tr>
<td>EAP products</td>
<td>13.3</td>
<td>22.8%</td>
<td>55.4</td>
<td>6.0%</td>
</tr>
<tr>
<td>ASO products</td>
<td>30.9</td>
<td>52.9%</td>
<td>101.7</td>
<td>11.1%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>58.4</strong></td>
<td><strong>100.0%</strong></td>
<td><strong>$917.3</strong></td>
<td><strong>100.0%</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Programs</th>
<th>Covered Lives</th>
<th>Percent</th>
<th>Revenue (in millions)</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Six Months Ended June 30, 2006</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Risk-Based products</td>
<td>9.1</td>
<td>21.4%</td>
<td>$648.1</td>
<td>83.1%</td>
</tr>
<tr>
<td>EAP products</td>
<td>13.6</td>
<td>32.0%</td>
<td>54.5</td>
<td>7.0%</td>
</tr>
<tr>
<td>ASO products</td>
<td>19.8</td>
<td>46.6%</td>
<td>76.8</td>
<td>9.9%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>42.5</strong></td>
<td><strong>100.0%</strong></td>
<td><strong>$779.4</strong></td>
<td><strong>100.0%</strong></td>
</tr>
</tbody>
</table>

Acquisition of National Imaging Associates

On January 31, 2006, the Company acquired all of the outstanding stock of NIA, a privately held radiology benefits management ("RBM") firm headquartered in Hackensack, New Jersey, for approximately $121 million in cash, after giving effect to cash acquired in the transaction, and NIA became a wholly owned subsidiary of Magellan.
NIA manages diagnostic imaging services for health plans to ensure that such services are clinically appropriate and cost effective. Currently, all of NIA’s management services are on a non-risk, ASO basis. The Company believes that NIA is the largest RBM manager in the country with approximately 17.9 million covered lives under contract as of June 30, 2006. The Company reports the results of operations of NIA as a separate segment entitled Radiology Benefits Management.

Acquisition of ICORE Healthcare, LLC

On June 28, 2006, the Company entered into a definitive agreement to acquire all of the outstanding ownership interests of ICORE, a privately held specialty pharmaceutical management firm headquartered in Orlando, Florida. Under the terms of the definitive agreement, the Company will pay a base price of approximately $210 million, before giving effect to cash acquired in the transaction, and may be required to pay a potential earn-out of up to $75 million to the owners of ICORE, all of whom are members of ICORE’s management team. The base price is payable in cash of approximately $186 million and, through a reinvestment, in restricted stock of approximately $24 million, which restricted stock will vest fifty percent each on the second and third anniversaries of the date of grant, provided the individuals do not terminate their employment prior to each such anniversary. The portion of the base price paid in restricted stock will be treated as compensation expense and not as purchase price. Of the cash portion of the purchase price, $25 million will be held back by the Company for three years to cover any indemnity claims under the definitive agreement, and the remaining $161 million, as well as transaction and other related costs, will be paid at closing. The earn-out will be comprised of two parts; up to $25 million based on earnings targets, as defined, for the 18-month period ending December 31, 2007 and up to $50 million based on earnings targets, as defined, in 2008. The earn-out, if earned, is payable 33 percent in cash and 67 percent in restricted stock that will vest over two years after issuance. The earn-out will be paid to the five executives of ICORE, who will become employees of the Company. Upon achieving the targets, the earn-out payments will be treated as compensation expense and not as additional purchase price.

ICORE works with health plans to manage specialty drugs used in the treatment of cancer, multiple sclerosis, hemophilia, infertility, rheumatoid arthritis, chronic forms of hepatitis and other diseases. ICORE holds contracts with approximately 36 health plans with approximately 60 million covered lives under contract in commercial, Medicare and Medicaid programs at June 30, 2006. The Company will report the results of operations of ICORE as a separate segment entitled Specialty Pharmaceutical Management. All material closing conditions for the transaction involving third parties have been met, and the Company expects that the transaction will be consummated on July 31, 2006.

Business Segments

Health Plan. The Managed Behavioral Healthcare Health Plan segment (“Health Plan”) generally reflects managed behavioral healthcare services provided under contracts with managed care companies, health insurers and other health plans. Health Plan’s contracts encompass both risk-based and ASO contracts for commercial, Medicaid and Medicare members of the health plan. Although certain health plans provide their own managed behavioral healthcare services, many health plans “carve out” behavioral healthcare from their general healthcare services and subcontract such services to managed behavioral healthcare companies such as the Company. In Health Plan, the Company’s members are the beneficiaries of the health plan (the employees and dependents of the customer of the health plan), for which the behavioral healthcare services have been carved out to the Company. Health Plan managed the behavioral health benefits of approximately 26.8 million covered lives as of June 30, 2006.
**Employer.** The Managed Behavioral Healthcare Employer segment ("Employer") generally reflects the provision of EAP services, managed behavioral healthcare services and integrated products under contracts with employers, including corporations and governmental agencies, and labor unions. Employer managed behavioral healthcare services are primarily ASO products. Employer provided these services for approximately 13.8 million covered lives as of June 30, 2006.

**Public Sector.** The Managed Behavioral Healthcare Public Sector segment ("Public Sector") generally reflects managed behavioral healthcare services provided to Medicaid recipients under contracts with state and local governmental agencies. Public Sector contracts encompass both risk-based and ASO contracts. Public Sector provided these services for approximately 1.9 million covered lives as of June 30, 2006.

**Radiology Benefits Management.** The Company’s Radiology Benefits Management segment generally reflects the management of diagnostic imaging services on a non-risk basis for health plans to ensure that such services are clinically appropriate and cost effective. The Company’s Radiology Benefits Management segment managed the benefits of approximately 17.9 million covered lives as of June 30, 2006.

**Corporate and Other.** This segment of the Company is comprised primarily of operational support functions such as sales and marketing and information technology, as well as corporate support functions such as executive, finance, human resources and legal.

**Significant Customers**

The Company’s contracts with the State of Tennessee’s TennCare program ("TennCare") and with subsidiaries of WellPoint, Inc. ("WellPoint"), each generated revenues that exceeded, in the aggregate, ten percent of consolidated net revenues for each of the three months and six months ended June 30, 2005 and 2006. The Company also has a significant concentration of business from individual counties which are part of the Pennsylvania Medicaid program.

The Company provides managed behavioral healthcare services for TennCare, both through contracts held by the Company’s wholly owned subsidiary Tennessee Behavioral Health, Inc. ("TBH") and through a contract held by Premier Behavioral Health Systems of Tennessee, LLC (“Premier”), a joint venture in which the Company owned a fifty percent interest. In addition, the Company contracts with Premier to provide certain services to the joint venture. The Company consolidates the results of operations of Premier, including revenue and cost of care, in the Company’s consolidated statements of income. On April 11, 2006, the Company purchased the other fifty percent interest in Premier for $1.5 million, so that Premier is now a wholly-owned subsidiary of the Company. TennCare has divided its program into three regions, and the Company’s TennCare contracts, which extend through June 30, 2007, currently encompass all of the TennCare membership for all three regions. The Company recorded revenue of $113.6 million and $226.7 million during the three months and six months ended June 30, 2005, respectively, and $101.8 million and $210.3 million during the three months and six months ended June 30, 2006, respectively, from its TennCare contracts.

On April 7, 2006, TennCare issued a Request for Proposals (“RFP”) for the management of the integrated delivery of behavioral and physical medical care to TennCare enrollees in the Middle region by managed care organizations. The RFP states that the start date of any such contract awarded pursuant to the RFP is expected to be April 1, 2007. Because the Company’s contracts with TennCare can be terminated by TennCare prior to June 30, 2007, the contract for the Middle region would be terminated by TennCare should an implementation occur prior to June 30, 2007 of any contract awarded pursuant to the RFP. On July 26, 2006, TennCare announced the two winning bidders to the RFP process. The Company had not partnered with either of these bidders. For the three months and six months ended June 30, 2006,
revenue derived from TennCare enrollees residing in the Middle region amounted to $36.8 million and $77.2 million, respectively.

Total revenue from the Company’s contracts with WellPoint approximated $54.6 million and $104.4 million during the three months and six months ended June 30, 2005, respectively, and approximated $50.4 million and $98.4 million during the three months and six months ended June 30, 2006, respectively. Included in the revenue amount for the three months and six months ended June 30, 2006 is revenue of $3.8 million and $6.2 million from contracts that NIA has with WellPoint. The majority of the Company’s managed behavioral healthcare contracts with WellPoint have terms that extend through December 31, 2007.

The Company derives a significant portion of its revenue from contracts with various counties in the State of Pennsylvania (the “Pennsylvania Counties”). Although these are separate contracts with individual counties, they all pertain to the Pennsylvania Medicaid program. Revenues from the Pennsylvania Counties in the aggregate totaled $54.0 million and $105.5 million in the three months and six months ended June 30, 2005, respectively and $61.9 million and $124.0 million in the three months and six months ended June 30, 2006, respectively.

The Company recorded net revenue from Aetna, Inc. (“Aetna”) of $60.7 million and $122.6 million for the three months and six months ended June 30, 2005, respectively, which represented in excess of ten percent of the consolidated revenues of the Company for such periods. The Company’s contract with Aetna terminated on December 31, 2005. During the three months and six months ended June 30, 2006, the Company recognized $0.8 million and $5.4 million of revenue related to the performance of one-time, transitional activities associated with the contract termination.

Off-Balance Sheet Arrangements

The Company does not maintain any off-balance sheet arrangements that have, or are reasonably likely to have, a current or future effect on the Company’s finances that is material to investors.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Except as noted below, the Company’s critical accounting policies are summarized in the Company’s Annual Report on Form 10-K, filed with the SEC on March 8, 2006.

Stock-based compensation

Effective January 1, 2006, the Company adopted the fair value recognition provisions of Statement of Financial Accounting Standards (“SFAS”) No. 123 (revised 2004) “Share-Based Payment” (“SFAS 123R”), using the modified prospective transition method and therefore has not restated results for prior periods. Under this transition method, stock-based compensation expense for the six months ended June 30, 2006 includes compensation expense for all stock-based compensation awards granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123, “Accounting for Stock-Based Compensation” (“SFAS 123”). Stock-based compensation expense for all stock-based compensation awards granted after January 1, 2006 is based on the grant date fair value estimated in accordance with the provisions of SFAS 123R. The Company recognizes these compensation costs on a straight-line basis over the requisite service period, which is generally the vesting term ranging from three to four years. Prior to the adoption of SFAS
123R, the Company recorded stock-based compensation under Accounting Principles Board (“APB”) Opinion No. 25, “Accounting for Stock Issued to Employees” (“APB 25”).

The Company estimates the fair value of stock options using the Black-Scholes-Merton option pricing model that employs the following key assumptions: Expected volatility is based on the annualized daily historical volatility of the Company’s stock price, over the expected life of the option. Management determined that volatility based on actively traded equities of companies that are similar to the Company is a better indicator of expected volatility and future stock price trends than historical Company volatility, due to the lack of sufficient history of the Company subsequent to the Company’s emergence from bankruptcy. Expected term of the option is based on historical employee stock option exercise behavior and the vesting terms of the respective option. Risk-free interest rates are based on the U.S. Treasury yield in effect at the time of grant.

SFAS 123R also requires the Company to recognize compensation expense for only the portion of options, restricted stock or restricted stock units that are expected to vest. Therefore, estimated forfeiture rates are derived from historical employee termination behavior. The Company’s estimated forfeiture rate for the six months ended June 30, 2006 is four percent. If the actual number of forfeitures differs from those estimated, additional adjustments to compensation expense may be required in future periods. If vesting of such an award is conditioned upon the achievement of performance goals, compensation expense during the performance period is estimated using the most probable outcome of the performance goals, and adjusted as the expected outcome changes.

Goodwill

Goodwill is accounted for in accordance with SFAS No. 142, “Goodwill and Other Intangible Assets” (“SFAS 142”). Pursuant to SFAS 142, the Company is required to test its goodwill for impairment on at least an annual basis. The Company has selected October 1 as the date of its annual impairment test. The balance of goodwill of $290.2 million at December 31, 2005 was allocated entirely to the Health Plan segment. At June 30, 2006, approximately $105.6 million of goodwill was allocated to the Radiology Benefits Management segment, and the remaining $261.2 million was allocated to the Health Plan segment.

Factors Affecting Comparability

As a result of the Company’s January 31, 2006 acquisition of NIA, the Company’s results of operations for the three months and six months ended June 30, 2005 are not comparable to the three months and six months ended June 30, 2006.

Results of Operations

The Company evaluates performance of its segments based on profit or loss from continuing operations before depreciation and amortization, interest expense, interest income, stock compensation expense, gain on sale of assets, income taxes and minority interest (“Segment Profit”). Management uses Segment Profit information for internal reporting and control purposes and considers it important in making decisions regarding the allocation of capital and other resources, risk assessment and employee compensation, among other matters. Intersegment sales and transfers are not significant.
The following tables summarize, for the periods indicated, operating results by business segment (in thousands):

<table>
<thead>
<tr>
<th>Three Months Ended June 30, 2005</th>
<th>Health Plan</th>
<th>Employer</th>
<th>Public and Plan</th>
<th>Corporate and Other</th>
<th>Consolidated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net revenue</td>
<td>$233,494</td>
<td>$31,741</td>
<td>$199,309</td>
<td>$—</td>
<td>$464,544</td>
</tr>
<tr>
<td>Cost of care</td>
<td>132,142</td>
<td>7,786</td>
<td>176,993</td>
<td>—</td>
<td>316,921</td>
</tr>
<tr>
<td>Direct service costs</td>
<td>42,296</td>
<td>16,430</td>
<td>7,614</td>
<td>—</td>
<td>66,340</td>
</tr>
<tr>
<td>Other operating expenses</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>23,861</td>
</tr>
<tr>
<td>Equity in earnings of unconsolidated subsidiaries</td>
<td>(1,503)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>(1,503)</td>
</tr>
<tr>
<td>Segment profit (loss)</td>
<td>$60,559</td>
<td>$7,525</td>
<td>$14,702</td>
<td>—</td>
<td>$58,925</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Three Months Ended June 30, 2006</th>
<th>Health Plan</th>
<th>Employer</th>
<th>Public and Plan</th>
<th>Corporate and Other</th>
<th>Consolidated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net revenue</td>
<td>$159,381</td>
<td>$32,057</td>
<td>$195,066</td>
<td>$12,429</td>
<td>$398,933</td>
</tr>
<tr>
<td>Cost of care</td>
<td>89,899</td>
<td>6,911</td>
<td>165,896</td>
<td>—</td>
<td>262,706</td>
</tr>
<tr>
<td>Direct service costs</td>
<td>25,516</td>
<td>17,427</td>
<td>8,918</td>
<td>10,130</td>
<td>61,991</td>
</tr>
<tr>
<td>Other operating expenses</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>24,113</td>
</tr>
<tr>
<td>Segment profit (loss)</td>
<td>$43,966</td>
<td>$7,719</td>
<td>$20,252</td>
<td>$2,299</td>
<td>$50,123</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Six Months Ended June 30, 2005</th>
<th>Health Plan</th>
<th>Employer</th>
<th>Public and Plan</th>
<th>Corporate and Other</th>
<th>Consolidated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net revenue</td>
<td>$458,396</td>
<td>$63,401</td>
<td>$395,501</td>
<td>$—</td>
<td>$917,298</td>
</tr>
<tr>
<td>Cost of care</td>
<td>253,870</td>
<td>15,646</td>
<td>351,613</td>
<td>—</td>
<td>621,129</td>
</tr>
<tr>
<td>Direct service costs</td>
<td>81,878</td>
<td>32,135</td>
<td>15,201</td>
<td>—</td>
<td>129,214</td>
</tr>
<tr>
<td>Other operating expenses</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>49,708</td>
</tr>
<tr>
<td>Equity in earnings of unconsolidated subsidiaries</td>
<td>(2,952)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>(2,952)</td>
</tr>
<tr>
<td>Segment profit (loss)</td>
<td>$125,600</td>
<td>$15,620</td>
<td>$28,687</td>
<td>$49,708</td>
<td>$120,199</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Six Months Ended June 30, 2006</th>
<th>Health Plan</th>
<th>Employer</th>
<th>Public and Plan</th>
<th>Corporate and Other</th>
<th>Consolidated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net revenue</td>
<td>$317,168</td>
<td>$65,237</td>
<td>$396,965</td>
<td>$20,159</td>
<td>$799,529</td>
</tr>
<tr>
<td>Cost of care</td>
<td>176,175</td>
<td>15,066</td>
<td>341,300</td>
<td>—</td>
<td>532,541</td>
</tr>
<tr>
<td>Direct service costs</td>
<td>51,849</td>
<td>34,122</td>
<td>16,980</td>
<td>16,381</td>
<td>119,332</td>
</tr>
<tr>
<td>Other operating expenses</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>48,740</td>
</tr>
<tr>
<td>Equity in earnings of unconsolidated subsidiaries</td>
<td>(390)</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>(390)</td>
</tr>
<tr>
<td>Segment profit (loss)</td>
<td>$89,534</td>
<td>$16,049</td>
<td>$38,685</td>
<td>$3,778</td>
<td>$99,306</td>
</tr>
</tbody>
</table>
The following table reconciles Segment Profit to consolidated income from continuing operations before income taxes and minority interest (in thousands):

<table>
<thead>
<tr>
<th></th>
<th>Three Months Ended June 30</th>
<th>Six Months Ended June 30</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2005</td>
<td>2006</td>
</tr>
<tr>
<td>Segment Profit</td>
<td>$58,925</td>
<td>$50,123</td>
</tr>
<tr>
<td>Depreciation and amortization</td>
<td>(13,573)</td>
<td>(11,333)</td>
</tr>
<tr>
<td>Interest expense</td>
<td>(8,611)</td>
<td>(1,721)</td>
</tr>
<tr>
<td>Interest income</td>
<td>3,899</td>
<td>4,921</td>
</tr>
<tr>
<td>Stock compensation expense</td>
<td>(4,419)</td>
<td>(6,594)</td>
</tr>
<tr>
<td>Gain on sale of assets</td>
<td>—</td>
<td>403</td>
</tr>
<tr>
<td>Income from continuing operations before income taxes and minority interest</td>
<td>$36,221</td>
<td>$35,799</td>
</tr>
</tbody>
</table>

Quarter ended June 30, 2006 (“Current Year Quarter”), compared to the quarter ended June 30, 2005 (“Prior Year Quarter”)

**Health Plan**

**Net Revenue**

Net revenue related to Health Plan decreased by 31.7 percent or $74.1 million from the Prior Year Quarter to the Current Year Quarter. The decrease in revenue is mainly due to terminated contracts of $86.8 million and other net unfavorable decreases of $0.2 million, which decreases were partially offset by increased membership from existing contracts of $5.0 million, new business of $7.1 million, and revenue in the Current Year Quarter of $0.8 million related to one-time transitional activities associated with the termination of the Aetna contract.

**Cost of Care**

Cost of care decreased by 32.0 percent or $42.2 million from the Prior Year Quarter to the Current Year Quarter. The decrease in cost of care is primarily due to terminated contracts of $53.4 million, favorable prior period medical claims development recorded in the Current Year Quarter of $4.8 million, and unfavorable prior period medical claims development recorded in the Prior Year Quarter of $4.8 million, which decreases were partially offset by care trends, change in mix of products and other net variances of $9.3 million, new risk business of $6.8 million, increased membership from existing customers of $2.9 million, and unfavorable care development for the Prior Year Quarter which was recorded after the Prior Year Quarter of $1.8 million. Cost of care decreased as a percentage of risk revenue to 70.2 percent in the Current Year Quarter from 70.7 percent in the Prior Year Quarter, mainly due to care trends and changes in business mix resulting primarily from the terminated contracts. For further discussion of Health Plan care trends, see “Outlook—Results of Operations” below.

**Direct Service Costs**

Direct service costs decreased by 39.7 percent or $16.8 million from the Prior Year Quarter to the Current Year Quarter. The decrease in direct service costs is primarily due to terminated contracts and cost-cutting and operating efficiency efforts by the Company. Direct service costs decreased as a percentage of revenue from 18.1 percent in the Prior Year Quarter to 16.0 percent for the Current Year Quarter, mainly due to the cost-cutting and operating efficiency efforts of the Company.
**Equity in Earnings of Unconsolidated Subsidiaries**

The Company recorded approximately $1.5 million of equity in earnings of unconsolidated subsidiaries in the Prior Year Quarter. The Company sold its equity interest in Royal Health Care, LLC (“Royal”) effective February 6, 2006.

**Employer**

*Net Revenue*

Net revenue related to Employer increased by 1.0 percent or $0.3 million from the Prior Year Quarter to the Current Year Quarter. The increase in revenue is mainly due to increased membership from existing customers of $1.2 million, revenue from new customers of $0.4 million, and other net favorable increases of $1.1 million, which increases were partially offset by terminated contracts of $2.4 million.

*Cost of Care*

Cost of care decreased by 11.2 percent or $0.9 million from the Prior Year Quarter to the Current Year Quarter. The decrease in cost of care is mainly due to favorable prior period medical claims development recorded in the Current Year Quarter of $0.7 million and favorable care trends and other net variances of $0.2 million. Cost of care decreased as a percentage of risk revenue from 27.8 percent in the Prior Year Quarter to 24.7 percent in the Current Year Quarter, mainly due to favorable prior period medical claims development recorded in the Current Year Quarter.

*Direct Service Costs*

Direct service costs increased by 6.1 percent or $1.0 million from the Prior Year Quarter to the Current Year Quarter. The increase is primarily due to expense related to services and support required for Hurricane Katrina victims and related activities in the Current Year Quarter, which also caused direct service costs to increase as a percentage of revenue from 51.8 percent for the Prior Year Quarter to 54.4 percent in the Current Year Quarter.

**Public Sector**

*Net Revenue*

Net revenue related to Public Sector decreased by 2.1 percent or $4.2 million from the Prior Year Quarter to the Current Year Quarter. This decrease is primarily due to net membership decreases of $10.5 million (mainly related to TennCare disenrollment that occurred in late fiscal 2005), contract changes of $1.7 million, and terminated contracts of $0.9 million, which decreases were partially offset by favorable rate changes of $7.7 million and other net increases of $1.2 million.

*Cost of Care*

Cost of care decreased by 6.3 percent or $11.1 million from the Prior Year Quarter to the Current Year Quarter. This decrease is primarily due to decreases in membership of $9.8 million, contract changes of $4.3 million, terminated contracts of $0.8 million, and care trends and other net variances of $0.5 million, which decreases were partially offset by care associated with rate changes for contracts that have minimum cost of care requirements of $4.3 million. Cost of care decreased as a percentage of risk revenue from 89.2 percent in the Prior Year Quarter to 85.6 percent in the Current Year Quarter mainly due to contract changes and rate increases in excess of care trend.
Direct Service Costs

Direct service costs increased by 17.1 percent or $1.3 million from the Prior Year Quarter to the Current Year Quarter. The increase in direct service costs was primarily due to costs associated with the TennCare pharmaceutical pilot contract and inflationary cost increases. As a percentage of revenue, direct service costs increased from 3.8 percent in the Prior Year Quarter to 4.6 percent in the Current Year Quarter primarily due to the costs associated with the TennCare pilot contract (which does not generate revenue).

Radiology Benefits Management

Net Revenue

Net revenue related to the Radiology Benefits Management segment was $12.4 million for the Current Year Quarter. As discussed above, the acquisition of NIA closed on January 31, 2006 and thus the Prior Year Quarter does not include any operating results for this segment of the Company.

Direct Service Costs

Direct service costs were $10.1 million for the Current Year Quarter. As a percentage of revenue, direct service costs were 81.5 percent.

Corporate and Other

Other Operating Expenses

Other operating expenses related to the Corporate and Other segment increased by 1.1 percent or $0.3 million from the Prior Year Quarter to the Current Year Quarter. The increase resulted primarily from corporate costs related to NIA and inflationary increases, partially offset by efficiency improvements and other net variances. As a percentage of total net revenue, other operating expenses increased from 5.1 percent for the Prior Year Quarter to 6.0 percent for the Current Year Quarter primarily due to the reduction in revenue from lost business.

Depreciation and Amortization

Depreciation and amortization expense decreased by 16.5 percent or $2.2 million from the Prior Year Quarter to the Current Year Quarter, primarily due to certain assets becoming fully depreciated prior to the Current Year Quarter and intangible assets related to the Aetna contract being fully amortized at December 31, 2005.

Interest Expense

Interest expense decreased by 80.0 percent or $6.9 million from the Prior Year Quarter to the Current Year Quarter, mainly due to the redemption of the Senior Notes and the Aetna Notes in the fourth quarter of 2005.

Interest Income

Interest income increased by $1.0 million from the Prior Year Quarter to the Current Year Quarter, mainly due to an increase in yields on investments.
Other Items

The Company recorded approximately $4.4 million and $6.6 million of stock compensation expense in the Prior Year Quarter and Current Year Quarter, respectively, related to common stock and stock options granted to management. The increase is due primarily to the adoption of SFAS 123R effective January 1, 2006. See discussion of stock compensation expense in “Outlook—Results of Operations” below.

A gain on the disposition of assets of $0.4 million was recognized in the Current Year Quarter as a result of additional consideration received related to the disposition of Aetna assets.

Income Taxes

The Company’s effective income tax rate was 42.3 percent in the Prior Year Quarter (restated) and 43.5 percent in the Current Year Quarter. In accordance with American Institute of Certified Public Accountants (“AICPA”) Statement of Position (“SOP”) 90-7, “Financial Reporting by Entities in Reorganization Under the Bankruptcy Code” (“SOP 90-7”), subsequent (post-bankruptcy) utilization by the Company of deferred tax assets including NOLs, which existed at January 5, 2004 are accounted for as reductions to goodwill rather than income tax provision and, therefore, only benefit cash flows due to reduced tax payments. The Prior Year Quarter and Current Year Quarter effective income tax rates differ from the federal statutory income tax rates primarily due to state income taxes and permanent differences between book and tax income.

Discontinued Operations

The income in discontinued operations in the Prior Year Quarter is attributable to favorable settlements received in the Prior Year Quarter and changes in estimated reserves for various accrued liabilities.

Six months ended June 30, 2006 (“Current Year Period”), compared to the six months ended June 30, 2005 (“Prior Year Period”)

Health Plan

Net Revenue

Net revenue related to Health Plan decreased by 30.8 percent or $141.2 million from the Prior Year Period to the Current Year Period. The decrease in revenue is mainly due to terminated contracts of $173.1 million, which decrease was partially offset by increased membership from existing contracts of $10.1 million, new business of $13.7 million, revenue in the Current Year Period of $5.4 million related to one-time transitional activities associated with the termination of the Aetna contract, and other net increases of $2.7 million.

Cost of Care

Cost of care decreased by 30.6 percent or $77.7 million from the Prior Year Period to the Current Year Period. The decrease in cost of care is primarily due to terminated contracts of $100.6 million, favorable prior period medical claims development recorded in the Current Year Period of $4.0 million, and unfavorable prior period medical claims development recorded in the Prior Year Period of $2.0 million, which decreases were partially offset by new risk business of $12.7 million, care trends, change in mix of products and other net increases of $7.2 million, increased membership from existing customers of $6.2 million, and unfavorable care development for the Prior Year Period which was recorded after the Prior Year Period of $2.8 million. Cost of care increased as a percentage of risk revenue to 70.0 percent in the Current Year Period from 69.4 percent in the Prior Year Period, mainly due to care trends and
changes in business mix resulting primarily from the terminated contracts. For further discussion of Health Plan care trends, see “Outlook—Results of Operations” below.

Direct Service Costs

Direct service costs decreased by 36.7 percent or $30.0 million from the Prior Year Period to the Current Year Period. The decrease in direct service costs is primarily due to terminated contracts and cost-cutting and operating efficiency efforts by the Company. Direct service costs decreased as a percentage of revenue from 17.9 percent in the Prior Year Period to 16.3 percent for the Current Year Period, mainly due to the cost-cutting and operating efficiency efforts of the Company.

Equity in Earnings of Unconsolidated Subsidiaries

The Company recorded approximately $3.0 million and $0.4 million of equity in earnings of unconsolidated subsidiaries in the Prior Year Period and Current Year Period, respectively. The Company sold its equity interest in Royal Health Care, LLC (“Royal”) effective February 6, 2006. Accordingly, the Current Year Period includes only one month of earnings in equity of Royal.

Employer

Net Revenue

Net revenue related to Employer increased by 2.9 percent or $1.8 million from the Prior Year Period to the Current Year Period. The increase in revenue is mainly due to increased membership from existing customers of $1.8 million, revenue from new customers of $0.7 million, increased revenue related to services and support required for Hurricane Katrina victims and related activities of $1.2 million, and other net favorable increases of $2.9 million, which increases were partially offset by terminated contracts of $4.8 million.

Cost of Care

Cost of care decreased by 3.7 percent or $0.6 million from the Prior Year Period to the Current Year Period. The decrease in cost of care is mainly due to terminated contracts of $0.9 million, which decrease was partially offset by care trends and other net increases of $0.3 million. Cost of care decreased as a percentage of risk revenue from 28.0 percent in the Prior Year Period to 26.6 percent in the Current Year Period, mainly due to changes in business mix.

Direct Service Costs

Direct service costs increased by 6.2 percent or $2.0 million from the Prior Year Period to the Current Year Period. The increase is primarily due to expense related to services and support required for Hurricane Katrina victims and related activities in the Current Year Period, which also caused direct service costs to increase as a percentage of revenue from 50.7 percent for the Prior Year Period to 52.3 percent in the Current Year Period.

Public Sector

Net Revenue

Net revenue related to Public Sector increased by 0.4 percent or $1.5 million from the Prior Year Period to the Current Year Period. This increase is primarily due to retrospective adjustments mainly related to membership recorded in the Current Year Period of $9.9 million and favorable rate changes of $17.8 million, which increases were partially offset by net membership decreases of $19.9 million (mainly

37
related to TennCare disenrollment that occurred in late fiscal 2005), contract changes of $3.5 million, terminated contracts of $1.9 million, and other net unfavorable variances of $0.9 million.

Cost of Care

Cost of care decreased by 2.9 percent or $10.3 million from the Prior Year Period to the Current Year Period. This decrease is primarily due to care associated with decreases in membership of $18.6 million, contract changes of $13.0 million, and terminated contracts of $1.6 million, which decreases were partially offset by retrospective membership adjustments recorded in the Current Year Period of $7.6 million and care trends and other net unfavorable variances of $15.3 million (including $10.5 million of care associated with rate changes for contracts that have minimum cost of care requirements). Cost of care decreased as a percentage of risk revenue from 89.3 percent in the Prior Year Period to 86.5 percent in the Current Year Period mainly due to contract changes and rate increases in excess of care trend.

Direct Service Costs

Direct service costs increased by 11.7 percent or $1.8 million from the Prior Year Period to the Current Year Period. The increase in direct service costs was primarily due to costs associated with the TennCare pharmaceutical pilot contract and inflationary cost increases. As a percentage of revenue, direct service costs increased from 3.8 percent in the Prior Year Period to 4.3 percent in the Current Year Period, primarily due to the costs associated with the TennCare pilot contract (which does not generate revenue).

Radiology Benefits Management

Net Revenue

Net revenue related to the Radiology Benefits segment was $20.2 million for the Current Year Period. As discussed above, the acquisition of NIA closed on January 31, 2006 and thus the Current Year Period includes five months of operating results and the Prior Year Period does not include any operating results for this segment of the Company.

Direct Service Costs

Direct service costs were $16.4 million for the Current Year Period. As a percentage of revenue, direct service costs were 81.3 percent.

Corporate and Other

Other Operating Expenses

Other operating expenses related to the Corporate and Other segment decreased by 1.9 percent or $1.0 million from the Prior Year Period to the Current Year Period. The decrease resulted primarily from efficiency improvements and other net favorable variances which were partially offset by corporate costs related to NIA and inflationary increases. As a percentage of total net revenue, other operating expenses increased from 5.4 percent for the Prior Year Period to 6.1 percent for the Current Year Period primarily due to the reduction in revenue from lost business.

Depreciation and Amortization

Depreciation and amortization expense decreased by 11.3 percent or $2.8 million from the Prior Year Period to the Current Year Period, primarily due to certain assets becoming fully depreciated prior to the Current Year Period and intangible assets related to the Aetna contract being fully amortized at December 31, 2005.
Interest Expense

Interest expense decreased by 78.6 percent or $13.6 million from the Prior Year Period to the Current Year Period, mainly due to the redemption of the Senior Notes and the Aetna Notes in the fourth quarter of 2005.

Interest Income

Interest income increased by $2.2 million from the Prior Year Period to the Current Year Period, mainly due to an increase in yields on investments.

Other Items

The Company recorded approximately $8.2 million and $12.1 million of stock compensation expense in the Prior Year Period and Current Year Period, respectively, related to common stock and stock options granted to management. The increase is due primarily to the adoption of SFAS 123R effective January 1, 2006. See discussion of stock compensation expense in “Outlook—Results of Operations” below.

A gain on the disposition of assets of $5.1 million was recognized in the Current Year Period mainly as a result of the Company’s sale of its equity interest in Royal.

Income Taxes

The Company’s effective income tax rate was 42.7 percent in the Prior Year Period (restated) and 43.9 percent in the Current Year Period. In accordance with SOP 90-7, subsequent (post-bankruptcy) utilization by the Company of deferred tax assets including NOLs, which existed at January 5, 2004 are accounted for as reductions to goodwill rather than income tax provision and, therefore, only benefit cash flows due to reduced tax payments. The Prior Year Period and Current Year Period effective income tax rates differ from the federal statutory income tax rates primarily due to state income taxes and permanent differences between book and tax income.

Discontinued Operations

The income in discontinued operations in the Prior Year Period is attributable to favorable settlements received in the Prior Year Period and changes in estimated reserves for various accrued liabilities.

Outlook—Results of Operations

The Company’s Segment Profit and net income are subject to significant fluctuations from period to period. These fluctuations may result from a variety of factors such as those set forth under Item 2—“Forward-Looking Statements” as well as a variety of other factors including: (i) changes in utilization levels by enrolled members of the Company’s risk-based contracts, including seasonal utilization patterns; (ii) contractual adjustments and settlements; (iii) retrospective membership adjustments; (iv) timing of award and implementation of new contracts; (v) enrollment changes; (vi) contract terminations; (vii) pricing adjustments upon contract renewals (and price competition in general) and (viii) changes in estimates regarding medical costs and incurred but not yet reported medical claims.

Care Trends. The Company expects that the Health Plan care trend factor for fiscal 2006 will be 6 to 8 percent. The Company estimates that the Public Sector care trend factor for fiscal 2006 will be 4 to 6 percent.
Stock Compensation. On January 1, 2006, the Company adopted SFAS 123R. Under SFAS 123R, the Company uses the Black-Scholes-Merton formula to estimate the value of stock options granted to employees. The Company estimates that stock compensation expense for fiscal 2006, exclusive of any expense that will result from the ICORE acquisition, will be approximately $27.0 million to $29.0 million.

Interest Rate Risk. Changes in interest rates affect interest income earned on the Company’s cash equivalents and investments, as well as interest expense on variable interest rate borrowings under the credit agreement with Deutsche Bank AG dated January 5, 2004, as amended (the “Credit Agreement”). Based on the amount of cash equivalents and investments and the borrowing levels under the Credit Agreement as of June 30, 2006, a hypothetical 10 percent increase or decrease in the interest rate associated with these instruments, with all other variables held constant, would not materially affect the Company’s future earnings and cash outflows.

Historical—Liquidity and Capital Resources

Operating Activities. Net cash provided by operating activities decreased by approximately $20.4 million from the Prior Year Period to the Current Year Period, primarily due to a decrease in segment profit between periods of $20.9 million, and payments of $24.4 million in the Current Year Period associated with claims run-out for terminated contracts, with such unfavorable variances partially offset by net positive working capital changes of $24.9 million (which mainly relates to favorable timing of cash flows from Public Sector segment regulated entities).

Investing Activities. The Company utilized $8.6 million and $8.9 million during the Prior Year Period and Current Year Period, respectively, for capital expenditures. The majority of capital expenditures for both periods related to management information systems and related equipment.

During the Current Year Period, the Company received proceeds of $22.2 million related to the sale of assets, mainly the sale of its investment in Royal. Additionally, during the Current Year Period, the Company used net cash of $120.7 million related to the acquisition of NIA.

During the Prior Year Period, the Company utilized net cash of $50.9 million for the purchase of “available-for-sale” investments and during the Current Year Period, the Company received net cash of $183.1 million from the net maturity of “available-for-sale” investments a portion of which was utilized to fund the NIA acquisition. The Company’s investments consist of U.S. government and agency securities, corporate debt securities and certificates of deposit.

During the Prior Year Period and the Current Year Period, the Company received proceeds of $7.0 million and $3.0 million, respectively, related to a previously outstanding $10.0 million note receivable.

Financing Activities. During the Prior Year Period, the Company repaid $11.2 million of indebtedness outstanding under the Credit Agreement and made payments on capital lease obligations of $2.3 million. In addition, the Company received $12.0 million from the exercise of stock options and warrants. During the Current Year Period, the Company repaid $12.5 million of indebtedness outstanding under the Credit Agreement and made payments on capital lease obligations of $0.2 million. In addition, the Company received $7.8 million from the exercise of stock options and warrants.

Outlook—Liquidity and Capital Resources

Liquidity. During fiscal 2006, the Company expects to fund its capital expenditures with cash from operations. The Company estimates that it will spend approximately $13 million to $23 million of additional funds in fiscal 2006 for capital expenditures. The Company does not anticipate that it will need to draw on amounts available under the revolving loan facility of the Credit Agreement for its operations, capital needs or debt service in fiscal 2006. The Company also currently expects to have adequate liquidity to satisfy its existing financial commitments over the periods in which they will become due. As discussed
previously, the acquisition of ICORE is expected to close on July 31, 2006. The Company believes that it will be able to fund from cash on hand the estimated cash portion of the purchase required at closing of $161 million, as well as all transaction and other related costs.

**Off-Balance Sheet Arrangements.** As of June 30, 2006, the Company has no off-balance sheet arrangements of a material significance.

**Restrictive Covenants in Debt Agreements.** The Credit Agreement contains covenants that limit management’s discretion in operating the Company’s business by restricting or limiting the Company’s ability, among other things, to:

- incur or guarantee additional indebtedness or issue preferred or redeemable stock;
- pay dividends and make other distributions;
- repurchase equity interests;
- make certain other payments;
- enter into sale and leaseback transactions;
- create liens;
- sell and otherwise dispose of assets;
- acquire or merge or consolidate with another company; and
- enter into some types of transactions with affiliates.

These restrictions could adversely affect the Company’s ability to finance future operations or capital needs or engage in other business activities that may be in the Company’s interest.

The Credit Agreement also requires the Company to comply with specified financial ratios and tests. Failure to do so, unless waived by the lenders under the Credit Agreement pursuant to its terms, would result in an event of default under the Credit Agreement. The Credit Agreement is guaranteed by most of the Company’s subsidiaries and is secured by most of the Company’s assets and the Company’s subsidiaries’ assets.

**Net Operating Loss Carryforwards.** The Company estimates that, as of December 2005, it had approximately $481 million of reportable NOLs. These estimated NOLs expire in 2010 through 2020 and are subject to examination and adjustment by the IRS. The Company’s utilization of NOLs became subject to limitation under Internal Revenue Code Section 382 upon emergence from bankruptcy, which affects the timing of the use of NOLs. At this time, the Company does not believe these limitations will materially limit the Company’s ability to use any NOLs before they expire. In accordance with SOP 90-7, subsequent (post-bankruptcy) utilization by the Company of NOLs that existed prior to the Company’s emergence from bankruptcy on January 5, 2004 will be accounted for as reductions to goodwill rather than income tax provision and, therefore, only benefit cash flows due to reduced tax payments. Although the Company has NOLs that may be available to offset future taxable income, the Company may be subject to Federal alternative minimum tax.

**Deferred Taxes.** The Company’s lack of a sufficient history of profitable operations subsequent to its emergence from bankruptcy has created uncertainty as to the Company’s ability to realize its deferred tax assets, inclusive of NOLs. Accordingly, as of December 31, 2005 and June 30, 2006, the Company’s valuation allowances were $167.2 million and $134.6 million, respectively, covering substantially all of its deferred tax assets, net of deferred tax liabilities and other tax contingencies. As of December 31, 2005 and June 30, 2006, net deferred tax assets, after reduction for valuation allowance, represent the Company’s estimate of those net tax assets which are “more likely than not” to be realizable. The Company continues to assess its
position relative to the potential future realization of the deferred tax assets for which valuation allowances have been recorded. If the Company subsequently determines that such deferred tax assets are more likely than not realizable, then the valuation allowances recorded for such deferred tax assets will be reversed. The reversal of valuation allowances for deferred tax assets that existed prior to the Company’s emergence from bankruptcy on January 5, 2004 would be recorded as a reduction to goodwill.

Recent Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board (“FASB”) issued FASB Interpretation (“FIN”) No. 48, “Accounting for Uncertainty in Income Taxes—An Interpretation of FASB Statement No. 109” (“FIN 48”), which prescribes a minimum recognition threshold and measurement methodology for tax positions taken or expected to be taken in a tax return. FIN 48 will be effective beginning January 1, 2007. The Company has not yet evaluated the impact of implementation of FIN 48 on its consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Changes in interest rates affect interest income earned on the Company’s cash equivalents and restricted cash and investments, as well as interest expense on variable interest rate borrowings under the Credit Agreement. Based on the Company’s investment balances, and the borrowing levels under the Credit Agreement as of June 30, 2006, a hypothetical 10 percent increase or decrease in the interest rate associated with these instruments, with all other variables held constant, would not materially affect the Company’s future earnings and cash outflows.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

The Company’s management evaluated, with the participation of the Company’s principal executive and principal financial officers, the effectiveness of the Company’s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of June 30, 2006. Based on their evaluation, the Company’s principal executive and principal financial officers concluded that the Company’s disclosure controls and procedures were effective as of June 30, 2006.

Changes in Internal Control over Financial Reporting

The Company had incorrectly reported the reversal of all valuation allowances for the use of deferred tax assets, other than NOLs, as a reduction of income tax expense for the year ended December 31, 2004, the nine months ended September 30, 2005, and each of the quarters in those periods. As a result, the Company has restated its consolidated financial statements for those periods. This restatement resulted in the reporting of a material weakness in internal controls over financial reporting in the Company’s 2005 Annual Report on Form 10-K. Management believes that the error was the result of an incorrect interpretation of very complex accounting guidance. Management has since reviewed and corrected its accounting policy for income taxes to accurately track and record the reversal of valuation allowances established under fresh start reporting prior to its emergence from bankruptcy with respect to deferred tax assets other than NOLs.

There has been no change in the Company’s internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the Company’s fiscal quarter ended June 30, 2006, that has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting.
PART II—OTHER INFORMATION

Item 1. Legal Proceedings.

The management and administration of the delivery of managed healthcare services entail significant risks of liability. From time to time, the Company is subject to various actions and claims arising from the acts or omissions of its employees, network providers or other parties. In the normal course of business, the Company receives reports relating to suicides and other serious incidents involving patients enrolled in its programs. Such incidents occasionally give rise to malpractice, professional negligence and other related actions and claims against the Company or its network providers. Many of these actions and claims received by the Company seek substantial damages and therefore require the defendant to incur significant fees and costs related to their defense. To date, claims and actions against the Company alleging professional negligence have not resulted in material liabilities and the Company does not believe that any such pending action against it will have a material adverse effect on the Company. However, there can be no assurance that pending or future actions or claims for professional liability (including any judgments, settlements or costs associated therewith) will not have a material adverse effect on the Company.

The Company is subject to or party to certain litigation and claims relating to its operations and business practices. Except as otherwise provided under the Third Joint Amended Plan of Reorganization, as modified and confirmed (the “Plan”), litigation asserting claims against the Company and its subsidiaries that were parties to the chapter 11 proceedings for pre-petition obligations (the “Pre-petition Litigation”) was enjoined as of January 5, 2005 (“the Effective Date”) as a consequence of the confirmation of the Plan and may not be pursued over the objection of Magellan or such subsidiary unless relief is provided from the effect of the injunction. The Company believes that the Pre-petition Litigation claims with respect to which distributions have been provided for under the Plan constitute general unsecured claims and, to the extent allowed by the Plan, would be resolved as other general unsecured creditor claims.

In the opinion of management, the Company has recorded reserves that are adequate to cover litigation, claims or assessments that have been or may be asserted against the Company, and for which the outcome is probable and reasonably estimable. Management believes that the resolution of such litigation and claims will not have a material adverse effect on the Company’s financial condition or results of operations; however, there can be no assurance in this regard.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None.

Item 3. Defaults Upon Senior Securities.

None.
Item 4. Submission of Matters to a Vote of Security Holders.

The annual meeting of shareholders of the Company was held on May 16, 2006 in connection with which proxies were solicited pursuant to Regulation 14A under the Securities Exchange Act of 1934. At the meeting, stockholders were asked to consider and vote upon (a) the election of two directors (“Proposal Number 1”); (b) approval of the 2006 Management Incentive Plan (“Proposal Number 2”); (c) approval of the 2006 Director Equity Compensation Plan (“Proposal Number 3”); (d) approval of the Magellan Health Services, Inc. Employee Stock Purchase Plan (“Proposal Number 4”); and (e) ratification of the appointment of Ernst & Young as the Company’s independent auditors for the fiscal year 2006 (“Proposal Number 5”).

(1) At the meeting, the two nominees of the Board of Directors (Barry Smith and René Lerer, M.D.) were elected as directors, with terms expiring in accordance with Magellan’s certificate of incorporation upon the 2009 annual meeting of stockholders and the election and qualification of their successors. The vote with respect to each nominee was as follows:

<table>
<thead>
<tr>
<th>Nominee</th>
<th>For</th>
<th>Withheld</th>
</tr>
</thead>
<tbody>
<tr>
<td>Barry M. Smith</td>
<td>32,622,210</td>
<td>1,558,035</td>
</tr>
<tr>
<td>René Lerer, M.D.</td>
<td>32,955,673</td>
<td>1,224,572</td>
</tr>
</tbody>
</table>

Other directors whose terms of office continued after the annual meeting are: Steven J. Shulman, Michael P. Ressner, Saul E. Burian, Michael Diament, William J. McBride, Robert M. LeBlanc and Allen F. Wise.

Proposal Number 2 was adopted with 24,268,922 votes cast for, and 9,903,272 votes cast against; in addition there were 8,051 abstentions on Proposal Number 2. Proposal Number 3 was adopted with 23,009,886 votes cast for, and 5,693,687 votes cast against; in addition there were 7,963 abstentions and 5,468,709 “broker non-votes” on Proposal Number 3. Proposal Number 4 was adopted with 28,013,845 votes cast for, and 692,104 votes cast against; in addition there were 5,588 abstentions and 5,468,708 “broker non-votes” on Proposal Number 4. Proposal Number 5 was adopted with 34,153,374 votes cast for, and 22,194 votes cast against; in addition there were 4,677 abstentions on Proposal Number 5.

Item 5. Other Information.

On July 24, 2006, the Management Compensation Committee of the Board of Directors of the Company approved certain amendments to the employment agreements of three executive officers, Daniel N. Grage, Chief Legal Officer, Eric Reimer, Chief Strategy and Development Officer, and Michael Majorik, Chief Sales and Marketing Officer, and also of one other officer, providing that in the event of termination of any such officer’s employment by the Company “without cause” or by the employee “with good reason” within 24 months of a “change in control” of the Company, as such terms are defined in the amendments, the affected officer would be entitled to the following:

(i) a pro-rata portion of target bonus for the year in which termination occurs, payable in a single installment immediately after termination,
(ii) 2 times the sum of (a) base salary plus (b) target bonus for such year, payable in a single cash installment immediately after termination,
(iii) immediate vesting of all stock options granted from January 4, 2004 and prior to March 10, 2005, and
(iv) payment by the Company of the Company’s portion of the cost for continued coverage under the Company’s health, dental and vision benefit programs under COBRA for 18 months after
termination of the officer’s employment if the officer elects post-employment coverage under such programs, provided the officer pays the
employee portion of the cost of such coverage,
as well as all compensation to which the officer had become entitled before the date of termination of employment, including any compensation which the officer is entitled to receive after termination of employment under any benefit program of the Company in which the officer participates.

The amendment, among other things, also provides that each such officer would be entitled to a “gross up” payment to cover any excise tax imposed in the event any portion of any such payments constitutes a “parachute payment” under Section 280G of the Internal Revenue Code (“IRC”) and extends the period of the non-competition covenant in the event of a termination of the officer “without cause” or a termination by the officer “with good reason” to the period in respect of which severance is paid to such officer as a result of the change in control.

The Management Compensation Committee also approved similar amendments to the employment agreements of certain other officers of the Company providing for similar benefits if any such officers are terminated “without cause” or terminate their employment for “good reason” within 18 months of a “change in control.” The amendments for these officers include a similar extension of their non-competition covenants as that provided for the executive officers referred to above, but do not include a “gross up” for excise taxes for “parachute payments” under IRC Section 280G.

Item 6. Exhibits

2.1 Agreement and Plan of Merger, dated as of June 27, 2006, among Magellan Health Services, Inc., Green Spring Health Services Inc., Magellan Sub Co. II, ICORE Healthcare LLC and Raju Mantena, as a representative of the unitholders of ICORE.

10.1 2006 Management Incentive Plan.

10.2 2006 Director Equity Compensation Plan.

10.3 2006 Employee Stock Purchase Plan.

10.4 Form of Amendment to Employment Agreement for Daniel N. Gregoire, Eric Reimer and Michael Majerik.

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
SIGNATURES

Pursuant to the requirements 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.

Date: July 28, 2006

MAGELLAN HEALTH SERVICES, INC.
(Registrant)

/s/ MARK S. DEMILIO
Mark S. Demilio
Executive Vice President and Chief Financial Officer (Principal Financial Officer and Duly Authorized Officer)
AGREEMENT AND PLAN OF MERGER

Dated as of June 27, 2006

among

MAGELLAN HEALTH SERVICES, INC.,
GREEN SPRING HEALTH SERVICES INC.,
MAGELLAN SUB CO. II, INC., AND
ICORE HEALTHCARE LLC
# TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>ARTICLE I</th>
<th>The Merger</th>
</tr>
</thead>
<tbody>
<tr>
<td>SECTION 1.1</td>
<td>The Merger</td>
</tr>
<tr>
<td>SECTION 1.2</td>
<td>Closing</td>
</tr>
<tr>
<td>SECTION 1.3</td>
<td>Effective Time</td>
</tr>
<tr>
<td>SECTION 1.4</td>
<td>Effects of the Merger</td>
</tr>
<tr>
<td>SECTION 1.5</td>
<td>Certificate of Formation and Limited Liability Company Agreement of the Surviving Company</td>
</tr>
<tr>
<td>SECTION 1.6</td>
<td>Management of the Surviving Company</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>ARTICLE II</th>
<th>Effect of the Merger on the Units and Capital Stock of the Company and Merger Sub; Merger Consideration; Exchange of Certificates</th>
</tr>
</thead>
<tbody>
<tr>
<td>SECTION 2.1</td>
<td>Effect on Capital Stock and Membership Interests</td>
</tr>
<tr>
<td>SECTION 2.2</td>
<td>Payment of Merger Consideration</td>
</tr>
<tr>
<td>SECTION 2.3</td>
<td>Adjustments to Company Units</td>
</tr>
<tr>
<td>SECTION 2.4</td>
<td>Guarantee of Parent</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>ARTICLE III</th>
<th>Representations and Warranties of the Company</th>
</tr>
</thead>
<tbody>
<tr>
<td>SECTION 3.1</td>
<td>Organization, Standing and Corporate Power</td>
</tr>
<tr>
<td>SECTION 3.2</td>
<td>Capitalization</td>
</tr>
<tr>
<td>SECTION 3.3</td>
<td>Authority; Noncontravention; Voting Requirements</td>
</tr>
<tr>
<td>SECTION 3.4</td>
<td>Governmental Approvals</td>
</tr>
<tr>
<td>SECTION 3.5</td>
<td>Financial Statements and Controls</td>
</tr>
<tr>
<td>SECTION 3.6</td>
<td>No Undisclosed Liabilities</td>
</tr>
<tr>
<td>SECTION 3.7</td>
<td>Absence of Certain Changes or Events</td>
</tr>
<tr>
<td>SECTION 3.8</td>
<td>Legal Proceedings</td>
</tr>
<tr>
<td>SECTION 3.9</td>
<td>Compliance With Laws</td>
</tr>
<tr>
<td>SECTION 3.10</td>
<td>Taxes.</td>
</tr>
<tr>
<td>SECTION 3.11</td>
<td>Employee Benefits and Labor Matters.</td>
</tr>
<tr>
<td>SECTION 3.12</td>
<td>Environmental Matters</td>
</tr>
<tr>
<td>SECTION 3.13</td>
<td>Contracts</td>
</tr>
<tr>
<td>SECTION 3.14</td>
<td>Title to Properties</td>
</tr>
<tr>
<td>SECTION</td>
<td>Description</td>
</tr>
<tr>
<td>---------</td>
<td>-----------------------------------------------------------------------------</td>
</tr>
<tr>
<td>3.15</td>
<td>Intellectual Property</td>
</tr>
<tr>
<td>3.16</td>
<td>Insurance</td>
</tr>
<tr>
<td>3.17</td>
<td>Brokers and Other Advisors</td>
</tr>
<tr>
<td>3.18</td>
<td>Health Care Regulatory Compliance</td>
</tr>
<tr>
<td>3.19</td>
<td>Accounts and Notes Receivable and Payable.</td>
</tr>
<tr>
<td>3.20</td>
<td>Related Party Transactions</td>
</tr>
<tr>
<td>3.21</td>
<td>Banks; Power of Attorney</td>
</tr>
<tr>
<td>3.22</td>
<td>Customers and Suppliers</td>
</tr>
<tr>
<td>3.23</td>
<td>Certain Payments</td>
</tr>
<tr>
<td>3.24</td>
<td>Full Disclosure</td>
</tr>
<tr>
<td>3.25</td>
<td>Employment Agreements With Key Employees</td>
</tr>
<tr>
<td>4.1</td>
<td>Organization, Standing and Corporate Power</td>
</tr>
<tr>
<td>4.2</td>
<td>Authority; Noncontravention</td>
</tr>
<tr>
<td>4.3</td>
<td>Governmental Approvals</td>
</tr>
<tr>
<td>4.4</td>
<td>Ownership and Operations of Acquiring Corp. and Merger Sub</td>
</tr>
<tr>
<td>4.5</td>
<td>Brokers and Other Advisors</td>
</tr>
<tr>
<td>4.6</td>
<td>Litigation</td>
</tr>
<tr>
<td>5.1</td>
<td>Conduct of Business</td>
</tr>
<tr>
<td>5.2</td>
<td>No Solicitation by the Company; Etc</td>
</tr>
<tr>
<td>5.3</td>
<td>Best Efforts</td>
</tr>
<tr>
<td>5.4</td>
<td>Public Announcements</td>
</tr>
<tr>
<td>5.5</td>
<td>Access to Information; Confidentiality</td>
</tr>
<tr>
<td>5.6</td>
<td>Notification of Certain Matters</td>
</tr>
<tr>
<td>5.7</td>
<td>Intentionally Omitted</td>
</tr>
<tr>
<td>5.8</td>
<td>Fees and Expenses</td>
</tr>
<tr>
<td>5.9</td>
<td>Change In Control Customer Contracts</td>
</tr>
<tr>
<td>5.10</td>
<td>Tax Matters</td>
</tr>
<tr>
<td>Section</td>
<td>Title</td>
</tr>
<tr>
<td>---------</td>
<td>-------</td>
</tr>
<tr>
<td>5.11</td>
<td>Employment Agreements</td>
</tr>
<tr>
<td>VI</td>
<td>Conditions Precedent</td>
</tr>
<tr>
<td>6.1</td>
<td>Conditions to Each Party’s Obligation to Effect the Merger</td>
</tr>
<tr>
<td>6.2</td>
<td>Conditions to Obligations of Parent, Acquiring Corp. and Merger Sub</td>
</tr>
<tr>
<td>6.3</td>
<td>Conditions to Obligation of the Company</td>
</tr>
<tr>
<td>6.4</td>
<td>Frustration of Closing Conditions</td>
</tr>
<tr>
<td>VII</td>
<td>Termination</td>
</tr>
<tr>
<td>7.1</td>
<td>Termination</td>
</tr>
<tr>
<td>7.2</td>
<td>Means and Effect of Termination</td>
</tr>
<tr>
<td>VIII</td>
<td>Survival of Representations, Warranties and Covenants; Indemnification</td>
</tr>
<tr>
<td>8.1</td>
<td>Survival of Representations, Warranties and Covenants</td>
</tr>
<tr>
<td>8.2</td>
<td>Indemnification</td>
</tr>
<tr>
<td>8.3</td>
<td>Indemnification Procedures</td>
</tr>
<tr>
<td>8.4</td>
<td>Reduction of the Deferred Payment Amount</td>
</tr>
<tr>
<td>8.5</td>
<td>Exclusivity of Remedy</td>
</tr>
<tr>
<td>8.6</td>
<td>Tax Treatment of Indemnity Payments</td>
</tr>
<tr>
<td>IX</td>
<td>Miscellaneous</td>
</tr>
<tr>
<td>9.1</td>
<td>Unitholder Representative</td>
</tr>
<tr>
<td>9.2</td>
<td>Amendment or Supplement</td>
</tr>
<tr>
<td>9.3</td>
<td>Extension of Time, Waiver, Etc</td>
</tr>
<tr>
<td>9.4</td>
<td>Assignment</td>
</tr>
<tr>
<td>9.5</td>
<td>Counterparts</td>
</tr>
<tr>
<td>9.6</td>
<td>Entire Agreement; No Third-Party Beneficiaries</td>
</tr>
<tr>
<td>9.7</td>
<td>Governing Law; Jurisdiction; Waiver of Jury Trial</td>
</tr>
<tr>
<td>9.8</td>
<td>Specific Enforcement</td>
</tr>
<tr>
<td>9.9</td>
<td>Consent to Jurisdiction</td>
</tr>
<tr>
<td>9.10</td>
<td>Notices</td>
</tr>
</tbody>
</table>
EXHIBITS

Exhibit 1.5(b) — Amended and Restated LLC Agreement of ICORE
Exhibit 2.1(d) — Calculation of Adjusted EBITDA
Exhibit 3.25 — List of Key Employees
Exhibit 6.2(a) — Certificate Regarding Financial Reporting

SCHEDULES

Schedule 3.1(b) — Ownership of Stock, Voting Securities or Equity Interests By ICORE
Schedule 3.2(a) — List of Unitholders and their Ownership Interests
Schedule 3.3(b) — Authorizations, Consents and Approvals
Schedule 3.3(c) — List of Unitholders Who Will Enter Into Subscription Agreements
Schedule 3.4 — Required Regulatory Filings and Approvals
Schedule 3.11(a) — Company Plans (Benefit) and Multi-Employer Plan
Schedule 3.11(i) — Action to Bring Company Plans into Conformity With Law
Schedule 3.13(a) — List of Contracts
Schedule 3.13(b) — Change in Control Customer Contracts
Schedule 3.13(c) — Change in Pricing and Other Terms of Contract
Schedule 3.15(b) — List of all Patents, Registered Marks & the Jurisdiction For Registration
Schedule 3.15(f) — List of all Software
Schedule 3.15(g) — List of Publicly Available Software
Schedule 3.16 — Insurance Policies
Schedule 3.18(a) — Material Healthcare Permits.
Schedule 3.18(b) — Licensing Matters
Schedule 3.18(c) — Third Party Payors
Schedule 3.18(i) — Financial Relationships
Schedule 3.20 — Related Party Transactions
Schedule 3.21 — List of Banks and Power of Attorney
Schedule 3.22(a) — List of Customers and Suppliers
Schedule 3.25 — Form of Employment Agreement with Key Employees
Schedule 5.1(c) — List of Benefit Plans
AGREEMENT AND PLAN OF MERGER

AGREEMENT AND PLAN OF MERGER, dated as of June 27, 2006 (this “Agreement”), is among MAGELLAN HEALTH SERVICES, INC., a Delaware corporation (“Parent”), GREEN SPRING HEALTH SERVICES INC., a Delaware corporation and wholly-owned subsidiary of Parent (“Acquiring Corp.”), MAGELLAN SUB CO. II, INC., a Delaware corporation and a wholly-owned Subsidiary of Acquiring Corp. (“Merger Sub”), ICORE HEALTHCARE, LLC, a Delaware limited liability company (the “Company”) and Raju Mantena, as the representative for the Company Unitholders (as defined below) (including any successor as representative for the Unitholders, the “Unitholder Representative”)

Certain terms used in this Agreement are used as defined in Section 9.12 below and all references herein to “Sections,” “Articles,” “Exhibits” or “Schedules” without further description shall refer to the sections, articles, exhibits or schedules of or to this Agreement.

WHEREAS, the Board of Directors of the Merger Sub and the Manager of the Company have approved and declared advisable, and the Board of Directors of Parent and Acquiring Corp. and Acquiring Corp. as the shareholder of Merger Sub has each approved, this Agreement and the merger of Merger Sub with and into the Company on the terms and subject to the conditions provided for in this Agreement; and

WHEREAS, the holders of the membership interests in the Company have, by written consent thereof or at a meeting duly convened, approved this Agreement and the merger of Merger Sub with and into the Company on the terms and subject to the conditions provided for in this Agreement;

NOW, THEREFORE, in consideration of the representations, warranties and covenants, and subject to the conditions, contained in this Agreement, and intending to be legally bound hereby, the parties hereto hereby agree as follows:

ARTICLE I
The Merger

SECTION 1.1. The Merger. Upon the terms and subject to the conditions set forth in this Agreement, and in accordance with the General Corporation Law of the State of Delaware (the “DGCL”) and the Delaware Limited Liability Company Act (the “LLC Act”), at the Effective Time Merger Sub shall be merged with and into the Company, the separate existence of Merger Sub shall thereupon cease, and the Company shall be the surviving company of the merger (the “Surviving Company”) of the merger (such transaction, the “Merger”).

SECTION 1.2. Closing. The closing of the Merger (the “Closing”) shall take place at 10:00 a.m. (New York City time) on a business day to be specified by Parent and reasonably acceptable to the Company, which date shall be no later than the
fourth business day after satisfaction or waiver of the conditions set forth in Article VI below (other than those conditions that by their nature are to be satisfied at the Closing, but subject to the satisfaction or waiver of such conditions), unless another time or date, or both, are agreed to in writing by the parties hereto. The date on which the Closing is held is herein referred to as the “Closing Date.” The Closing will be held at the offices of Weil, Gotshal & Manges LLP, 767 Fifth Avenue, New York, New York 10153, unless another place is agreed to by the parties hereto.

SECTION 1.3 Effective Time. Subject to the provisions of this Agreement, at the Closing the parties shall cause to be filed with the Office of the Secretary of State of the State of Delaware an appropriate certificate of merger, executed in accordance with the relevant provisions of the DGCL and the LLC Act, to effectuate the Merger (the “Certificate of Merger”). The Merger shall become effective upon the filing of the Certificate of Merger or at such later time as is agreed to by the parties hereto and specified in the Certificate of Merger (the time at which the Merger becomes effective is herein referred to as the “Effective Time”).

SECTION 1.4 Effects of the Merger. The Merger shall have the effects set forth in the DGCL and the LLC Act. Without limiting the generality of the foregoing, and subject thereto, at the Effective Time, all the properties, rights, privileges, powers and franchises of the Company and Merger Sub shall vest or remain vested, respectively, in the Surviving Company, and all debts, liabilities and duties of the Company and Merger Sub shall become or remain, respectively, the debts, liabilities and duties of the Surviving Company.

SECTION 1.5 Certificate of Formation and Limited Liability Company Agreement of the Surviving Company.

(a) The certificate of formation of the Company, as in effect immediately prior to the Effective Time, shall be the certificate of formation of the Surviving Company as of the Effective Time until thereafter amended as provided therein or by applicable Law.

(b) The limited liability company agreement of the Company, as in effect immediately prior to the Effective Time, shall be amended and restated at the Effective Time to read in its entirety, as amended and restated, as provided by Exhibit 1.5(b) and, commencing as of the Effective Time shall be the limited liability company agreement of the Surviving Company, until thereafter amended as provided therein or by applicable Law.

SECTION 1.6 Management of the Surviving Company. Commencing with the Effective Time, the Surviving Company shall be managed by or under the direction of its Board of Managers in accordance with the amended and restated limited liability company agreement of the Surviving Company, until said agreement is thereafter amended as provided therein or by applicable Law. The members of the Board of Managers of the Surviving Company at the Effective Time shall be as provided in Exhibit 1.5(b), until changed as provided in accordance with the amended and restated limited liability agreement of the Surviving Company. The officers of the Surviving Company at the Effective Time shall be as provided Exhibit 1.5(b).
ARTICLE II
Effect of the Merger on the Units and Capital Stock of the Company and Merger Sub; Merger Consideration; Exchange of Certificates

SECTION 2.1 Effect on Capital Stock and Membership Interests. At the Effective Time, by virtue of the Merger and without any action on the part of any holder of shares of common stock, par value $.01 per share, of the Merger Sub (the “Merger Sub Common Stock”) or the holders (the “Company Unitholders”) of Units of membership interest of the Company as determined in accordance with the operating agreement of the Company (the “Company Units”),

(a) Merger Sub Common Stock. Each share of Merger Sub Common Stock issued and outstanding immediately before the Effective Time shall be cancelled and converted into one newly issued unit of member interest in the Surviving Company, as such units of member interest are provided for by the amended and restated limited liability company agreement of the Surviving Company as in effect at the Effective Time. As of the Effective Time, the shares of Merger Sub Common Stock shall no longer be outstanding and shall automatically be canceled and shall cease to exist, and the holder or holders of such shares shall cease to have any rights with respect thereto, except the right to receive the units of member interest in the Surviving Company to be issued in consideration therefor as provided herein, without interest.

(b) Conversion of Company Units. Subject to the following provisions of this Section 2.1 and to Section 2.2, the Company Units issued and outstanding immediately before the Effective Time shall be cancelled and converted into the right to receive from the Acquiring Corp. in the manner hereinafter provided the following (in the aggregate with respect to all Company Units, the “Merger Consideration”): (i) the amount in cash, without interest, equal to $210,000,000 (the “Aggregate Initial Cash Purchase Price”), plus (ii) the Earn-out Consideration; provided, however, that the Merger Consideration shall be subject to reduction if and as provided by Article VIII. It is understood and agreed that, as provided by Section 2.2, the Aggregate Initial Cash Purchase Price will be paid in two installments, the first on or as soon as practicable after the Effective Time and the second on or as soon as practicable after the third anniversary of the Closing (as set forth in Section 2.2(a) below) and that the Company Unitholders may not be entitled to receive the full amount of the Aggregate Initial Cash Purchase Price or the Earn-out Consideration if and to the extent that any portion thereof is reduced as provided by Article VIII or if a Company Unitholder is required in accordance with Article VIII to return part of the Merger Consideration. As of the Effective Time, the Company Units shall no longer be outstanding and shall automatically be canceled and shall cease to exist, and the holders of Company Units

3
shall cease to have any rights with respect thereto, except the right to receive the Merger Consideration to be paid in consideration therefor as provided herein, without interest. In addition to the Aggregate Initial Cash Purchase Price and the Earn-out Consideration payable pursuant to this Section 2.1(b), Company Unitholders may also be entitled to additional amounts in accordance with Sections 2.2(a) to the extent the Deferred Payment includes an amount representing interest as provided by such Section.

(c) **Earn-out Consideration.** In addition to the Aggregate Initial Cash Purchase Price, Company Unitholders shall be entitled to receive from the Acquiring Corp., subject to the following terms and conditions of this Section 2.1 (including, without limitation, the restrictions contained in the last paragraph of this Section 2.1(c) and to Section 2.2, as part of the Merger Consideration the following (in the aggregate with respect to all Company Units, the "**Earn-out Consideration**"), provided, however, that the Earn-out Consideration shall be subject to reduction if and as provided by Article VIII:

(i) If, determined as provided in Section 2.1(d), the Company’s Adjusted EBITDA for the period from July 1, 2006 through December 31, 2006 exceeds $12,000,000 and the Company’s Adjusted EBITDA for 2007 exceeds $30,000,000, then the Company Unitholders immediately before the Effective Time shall be entitled to receive, in the aggregate, an additional amount equal to the sum of (A) the product of 0.75 multiplied by the amount by which the Company’s Adjusted EBITDA for the period from July 1, 2006 through December 31, 2006 exceeds $12,000,000 plus (B) the product of 5.0 multiplied by the amount by which the Company’s Adjusted EBITDA for 2007 exceeds $30,000,000; provided, however, that in no event shall the aggregate amount to be so received by Company Unitholders under this paragraph (i) exceed $25,000,000. Such Earn-out Consideration shall be divided among the Company Unitholders in accordance with either their Target Percentage Interests or, if Parent receives from the Unitholder Representative at least ten business days before the Closing a notice providing for the Earn-out Consideration to be divided among the Company Unitholders in different percentages, then in the percentages set forth in such notice (provided, however, that (1) such allocation shall be reasonably acceptable to Company Unitholder and (2) no Company Unitholder who held Class B Units of the Company immediately before the Effective Time shall be allocated a portion of the aggregate Earn-Out Consideration which is less than his respective Target Percentage Interest), which percentages may be revised prior to the First Earn-out Distribution Date or the Second Earn-out Distribution Date, as applicable, by the Unitholder Representative by notice given to Parent, subject to approval by Parent of such revised percentages (and provided, however, that no Company Unitholder who held Class B Units of the Company immediately before the Effective Time shall then be allocated a portion of the aggregate Earn-Out Consideration which is less than his respective Target Percentage Interest). The percentages in which payments of Earn-out Consideration are to be paid to Company Unitholders are hereinafter referred to as their **Earn-out Percentages.** Such Earn-out
Consideration shall be payable on the First Earn-out Distribution Date to each such Company Unitholder 33% in cash and 67% in Parent Shares, for which purpose Parent Shares shall be considered to have a value equal to the Fair Market Value of the Parent Shares on the First Earn-out Distribution Date, but such Parent Shares to be subject to the restrictions provided by Section 2.1(e).

(ii) If the Company’s Adjusted EBITDA for the period from July 1, 2006 through December 31, 2006 fails to exceed $12,000,000 but the Company’s Adjusted EBITDA for 2007 exceeds $30,000,000, then the Company Unitholders immediately before the Effective Time shall be entitled to receive in the aggregate, an additional amount equal to the product of 5.0 multiplied by the amount by which the Company’s Adjusted EBITDA for the period from July 1, 2006 through December 31, 2007 exceeds $42,000,000; provided, however, that in no event shall the aggregate amount to be so received by Company Unitholders under this paragraph (ii) exceed $25,000,000. Such Earn-out Consideration shall be divided among the Unitholders in accordance with their respective Earn-out Percentages as in effect at the time for such payment. Such Earn-out Consideration shall be payable on the First Earn-out Distribution Date to each such Company Unitholder 33% in cash and 67% in Parent Shares, for which purpose Parent Shares shall be considered to have a value equal to the Fair Market Value of the Parent Shares on the First Earn-out Distribution Date, but such Parent Shares to be subject to the restrictions provided by Section 2.1(e).

(iii) In addition, if the Company’s Adjusted EBITDA for 2008 exceeds $45,000,000, then the Company Unitholders immediately before the Effective Time shall be entitled to receive, in the aggregate, an additional amount equal to the product of 2.38 multiplied by the amount by which the Company’s Adjusted EBITDA for 2008 exceeds $45,000,000; provided, however, that in no event shall the aggregate amount to be so received by Company Unitholders under this paragraph (iii) exceed $50,000,000. Such Earn-out Consideration shall be divided among the Unitholders in accordance with their respective Earn-out Percentages as in effect at the time for such payment. Such Earn-out Consideration shall be payable on the Second Earn-out Distribution Date to each such Company Unitholder 33% in cash and 67% in Parent Shares, for which purpose Parent Shares shall be considered to have a value equal to the Fair Market Value of the Parent Shares on the Second Earn-out Distribution Date, but such Parent Shares to be subject to the restrictions provided by Section 2.1(e).

(iv) Notwithstanding the foregoing provisions of this Section 2.1(c), a Company Unitholder immediately before the Effective Time (1) shall only be entitled to receive any Earn-out Consideration on the First Earn-out Distribution Date if such Company Unitholder on such date is, and at all times from the Closing Date to the First-Earn-out Distribution Date was, an Employee in Good Standing of the Parent or a Subsidiary and (2) shall only be entitled to receive any Earn-out Consideration on the Second Earn-out Distribution Date, if such Company Unitholder on such date is, and at all times from the Closing Date to
the Second Earn-out Distribution Date was, an Employee in Good Standing of the Parent or a Subsidiary. A Company Unitholder shall be considered an “Employee in Good Standing” of the Parent or a Subsidiary from the Closing through the First Earn-out Distribution Date or the Second Earn-out Distribution Date, as the case may be, if such Company Unitholder (1) continued in the employ of the Company following the Closing to such date pursuant to his employment agreement referred to in Section 3.25 or (2) his employment pursuant to such agreement terminated or lapsed after the Closing and before such date for a “Qualifying Reason” as provided by such agreement or (3) during such period he was employed by the Parent or any other Subsidiary of the Parent other than the Company pursuant to an employment agreement providing that he or she will be considered an Employee in Good Standing of the Parent or a Subsidiary during such employment.

(v) It is understood and agreed that by reason of a forfeiture of Parent Shares in accordance with Section 2.1(e) and/or a reallocation of Additional Parent Shares as provided by Section 2.1(e), a Company Unitholder may ultimately retain a smaller portion, or receive a larger portion, of the Earn-out Consideration than its Earn-out Percentage of the aggregate Earn-out Consideration.

(d) Calculation of Adjusted EBITDA of the Company. For purposes of this Agreement, the Company’s Adjusted EBITDA for the periods referred to in Section 2.1(c) shall be determined in accordance with the provisions of Exhibit 2.1(d).

(e) Restrictions on Parent Shares Issued As Earn-out Consideration. Any Parent Shares issued to a Company Unitholder as Earn-out Consideration pursuant to paragraph (i) or (ii) of Section 2.3(c) shall be restricted as follows: (1) except as otherwise provided by the last sentence of this Section 2.1(e), without the prior written consent of the Parent (executed by an executive officer thereof), no Transfer of any of such Parent Shares shall be permitted until the first anniversary of the First Earn-out Distribution Date, after which time up to one-half of such Parent Shares may be Transferred, and no Transfer of the remainder of such Parent Shares shall be permitted until the second anniversary of the First Earn-out Distribution Date, after which time all of such Parent Shares may be Transferred, and (2) in the event at any time before the date such shares become Transferable, as provided in clause (1) of this sentence, such Company Unitholder shall cease to be an Employee in Good Standing of the Parent or a Subsidiary thereof, such Company Unitholder shall immediately, except as otherwise provided by the last sentence of this Section 2.1(e), as of such time, forfeit such Parent Shares to the Acquiring Corp. and shall deliver any certificates representing such shares, duly endorsed for transfer, to the Acquiring Corp. for no consideration. Any Parent Shares issued to a Company Unitholder as Earn-out Consideration pursuant to paragraph (iii) of Section 2.3(c) shall be restricted as follows: (1) except as otherwise provided by the last sentence of this Section 2.1(e), without the prior written consent of the Parent (executed by an executive officer thereof), no Transfer of any of such Parent Shares shall be permitted until the first anniversary of the Second Earn-out Distribution Date, after which time up to one-half of such Shares may be Transferred, and no Transfer of the remainder of such Parent Shares shall be permitted until the second anniversary of the Second Earn-out Distribution Date, after
which time all of such Parent Shares may be Transferred, and (2) in the event at any time before the date such shares become Transferable, as provided in clause (1) of this sentence, such Company Unitholder shall cease to be an Employee in Good Standing of the Parent or a Subsidiary thereof, such Company Unitholder shall immediately, except as otherwise provided by the last sentence of this Section 2.1(e), as of such time, forfeit such Parent Shares to the Acquiring Corp. and shall deliver any certificates representing such Shares, duly endorsed for transfer, to the Acquiring Corp., for no consideration. Notwithstanding the foregoing provisions of this Section 2.1(e), if and to the extent a Company Unitholder has in accordance with Section 2.1(e) been so issued a number of Parent Shares as part of the Earn-out Consideration which is in excess of his Target Percentage of all Parent Shares so issued as Earn-out Consideration (such shares in the case of such Company Unitholder, “Additional Parent Shares”), then (1) if Raju Mantena ceases to be an Employee in Good Standing before the date on which such Additional Parent Shares become Transferable, all such Company Unitholders shall forfeit such Additional Shares to the Acquiring Corp., which Shares may (but need not) be reallocated among the Company Unitholders who continue to be Employees in Good Standing, in the sole and absolute discretion of the Acquiring Corp. and (2) if the foregoing clause (1) is not applicable at the time, then if such a Company Unitholder ceases to be an Employee in Good Standing before the date on which such Additional Parent Shares become Transferable, such Company Unitholder shall forfeit such Additional Parent Shares to the Unitholder Representative, as agent for the Company Unitholders who continue to be Employees in Good Standing of Parent or a Subsidiary thereof (instead of to the Acquiring Corp.), and in either such case such Company Unitholder shall deliver any certificates representing such Additional Parent Shares that are to be forfeited, duly endorsed for transfer, to the Acquiring Corp. or the Unitholder Representative, as the case may be, for no consideration. Within 90 days after such a forfeiture of Additional Parent Shares to the Unitholder Representative, the Unitholder Representative may reallocate and transfer such forfeited Additional Parent Shares to Company Unitholders who continue to be at such time Employees in Good Standing of the Parent or a Subsidiary thereof (including the Unitholder Representative) as the Unitholder Representative determines to be appropriate after consultation with Parent; it being understood that the Unitholder Representative will not reallocate such Parent Shares in a manner to which Parent reasonably objects. Any such reallocation of Parent Shares among Company Unitholders shall be reflected in an amended notice signed by the Unitholder Representative and delivered to Parent and any Additional Parent Shares so reallocated shall remain in the hands of the Company Unitholder to whom they are reallocated subject to the same restrictions on transfer and forfeiture provided hereby as if such Additional Parent Shares had originally been issued to such Company Unitholder. Notwithstanding the foregoing provisions of this Section 2.1(e), (1) such Parent Shares shall be Transferable (A) in the event of the holder’s death, by will or the laws of descent and distribution or by a written beneficiary designation accepted by Parent, (B) by operation of law in connection with a merger, consolidation, recapitalization,
reclassification or exchange of Shares, reorganization or similar transaction involving the Company and affecting Parent Shares generally or (C) with the approval of Parent, to a member of the holder’s family, or a trust primarily for the benefit of the holder and/or one or more members of the holder’s family, or to a corporation, partnership or other entity primarily for the benefit of the holder and/or one or more such family members and/or trusts or (D) with the approval of the Parent, in another estate or personal financial planning transaction (provided, however, that in any such case the Parent Shares so Transferred shall remain subject in the hands of the Transferee to the restrictions on Transfer provided hereby and, except in the case of a Transfer referred to in the foregoing clause (A) of this sentence, shall remain subject to forfeiture upon the transferor Company Unitholder subsequently ceasing to be an Employee in Good Standing before the expiration of the period of restriction on Transfer of such Parent Shares, as provided by the first or second sentence of this paragraph and (2) no Transfer of such Parent Shares shall be permitted unless such Transfer (A) shall be registered under the Securities Act and registered or qualified under any applicable state securities law or the holder has established to the Parent’s reasonable satisfaction that the Transfer is exempt from such registration or qualification and (B) shall be made in accordance with any restrictions on Transfer of Parent Shares to which holder may be subject as an employee, officer and/or director of the Parent or a Subsidiary thereof by reason of federal or state securities laws and/or the policies regarding transactions in securities of the Parent from time to time adopted by the Parent and applicable to the holder. Except in respect of the foregoing restrictions on Transfer and forfeiture requirement, a holder of such Parent Shares shall be entitled to the benefit of, and to exercise, all rights, powers and privileges of ownership of such shares, including without limitation the right to receive dividends and distributions thereon, and to vote such shares and to exercise any rights of dissent or appraisal or to make any election attendant upon ownership of such shares; provided, however, that to the extent any dividend shall be paid or distribution made on such shares in any shares or securities of Parent or any Subsidiary of Parent during the period in which Transfer of such shares is restricted hereby, then such shares or securities shall be likewise restricted from Transfer and subject to forfeiture to the Acquiring Corp. For the avoidance of doubt, it is understood and agreed that, upon a Transfer of any such Parent Shares after the expiration of such restrictions on Transfer (or with such consent), the foregoing restrictions shall terminate as to the Transferee of such Parent Shares. Parent may legend any certificates representing such Parent Shares (or other shares or securities distributed in respect thereof) in such manner, or enter appropriate stop transfer instructions with any transfer agent or registrar, as may be reasonably determined by Parent to be appropriate to effectuate the provisions of this Section 2.1(e). Notwithstanding the foregoing provisions of this Section 2.1(e), (1) in the event the Acquiring Corp. is required to deposit with the Escrow Agent (or, in lieu thereof, deliver to the Unitholder Representative an irrevocable letter of credit) in respect of the amount of the Deferred Payment as provided by Section 2.2(a) and has failed to do so within 120 days after becoming required to do so or the Acquiring Corp. fails to make payment to the Company Unitholders of the Deferred Payment within five business days after becoming obligated to do so or (2) in the event a Company Unitholder terminates his employment as provided by his employment agreement referred to in Section 3.25 within
120 days following a Change of Control of Parent, any Parent Shares theretofore issued to a Company Unitholder as Earn-out Consideration shall no longer be subject to restrictions on transfer or to forfeiture as provided herein.

(f) **Successor Securities.** If there shall be any change in or exchange of the outstanding Parent Shares prior to the issuance of Parent Shares pursuant to Section 2.1(c), by reason of a recapitalization, reorganization or exchange of shares including any such change or exchange effectuated by an amendment of Parent’s certificate of incorporation or by a merger or consolidation, all references in this Agreement to “Parent Shares” shall likewise refer to the shares as so changed or the shares or other securities into which the Parent Shares are so changed or exchanged. The provision of this Section 2.1(f) shall apply to each such successive change or exchange.

(g) **Working Capital Payment and Adjustment.** In addition to the consideration payable to the Company Unitholders as provided by Section 2.1(b), the Acquiring Corp. will make the payments in respect of the Company’s “Working Capital” as of the Closing Date hereinafter in this Section 2.1(g) provided for.

(i) The Company’s “**Working Capital**” shall be in the amount (determined as hereinafter provided) by which the Company’s current assets exceed its current liabilities as of the Closing Date, as determined in accordance with GAAP consistently applied by the Company; it being understood, however, that in determining the Working Capital the amount owed on the note issued by the Company to Raju Mantena and outstanding on the date hereof (which on the date hereof approximates $2.45 million), will not be considered a current liability of the Company nor will any other amount owed by the Company to any Company Unitholder for borrowed money (the “**Working Capital Loans**”). The Company has provided Parent in writing its good faith estimate of the amount of its Working Capital as of March 31, 2006 and shall provide Parent in writing a good faith estimate of the amount of the Working Capital Loans as of the Closing Date, signed by its chief executive and chief financial officers, no later than three business days before the Closing Date, explaining any material change in the Company’s Working Capital since March 31, 2006.

(ii) The Acquiring Company will pay to the Company at the Closing, in respect of its Working Capital as of the Closing Date, in cash the amount of the Working Capital Loans as estimated by the Company as provided in paragraph (i) of this section. The Company will repay in their entirety, substantially simultaneously with the Closing, the Working Capital Loans.

(iii) After consulting with the Unitholder Representative, the Company not later than 90 days after the Closing shall provide the Acquiring Corp. and the Unitholder Representative with a revised estimate of the Company’s Working Capital as of the Closing Date (the "**Estimated Working Capital Amount**"), explaining any material change in the Company’s Working Capital as of the Closing Date as estimated before the Closing. On January 31, 2007, the
Acquiring Corp. shall pay to the Company Unitholders, divided among them in accordance with their respective Percentage Interests, the amount equal to $6,000,000 less the estimated amount of the Working Capital Loans paid by the Acquiring Corp. to the Company at the Closing.

(iv) As soon as practicable after the beginning of the thirteenth month after the Closing Date, the Company shall re-calculate its Working Capital as of the Closing Date taking into account all relevant post-Closing events until such time. Acquiring Corp. and the Unitholder Representative will cooperate with the Company in determining a mutually agreeable amount for the re-calculated Working Capital as of the Closing Date. In the event of a disagreement between the Unitholder Representative and Acquiring Corp. as to the Working Capital as of the Closing Date so re-calculated, the Unitholder Representative and Acquiring Corp. will jointly select a reasonably acceptable independent public accounting firm to determine the amount of the Working Capital as of the Closing Date, which determination shall be final and binding upon all parties in interest. Expenses relating to the independent public accounting firm shall be borne equally by the Acquiring Corp. and the Unitholder Representative. The difference, if any, between the recalculated Working Capital and the total amount of the payments on account of the Company’s Working Capital made by the Acquiring Corp. to the Company in accordance with paragraph (ii) of this section and made to the Company Unitholders in accordance with paragraph (iii) of this section will be promptly settled by either an additional cash payment to the Company Unitholders (divided among them in accordance with their Percentage Interests) by Acquiring Corp., if the difference is positive, or by a cash payment to Acquiring Corp. by the Unitholder Representative on behalf of all the Company Unitholders if the difference is negative. If any such settlement payment is not made within five business days of demand therefor, such payment shall bear interest at the prime rate as from time to time in effect (as published in The Wall Street Journal) plus 400 basis points from the date of demand to the date of payment. If such payment is payable to the Acquiring Corp. and is not paid upon demand, the Acquiring Corp. may elect by notice to the Unitholder Representative at any time before payment thereof is made to the Acquiring Corp. to reduce the amount of the Deferred Payment by the amount so owed to it.

(v) Notwithstanding the foregoing provisions of this Section 2.1(g), the maximum amount payable by Acquiring Corp. pursuant to paragraphs (iii) and (iv) of this section shall not exceed $25,000,000.

SECTION 2.2 Payment of Merger Consideration

(a) Acquiring Corp. shall simultaneously with the Closing (and subject to the satisfaction or waiver of the conditions to the Closing provided by Article VI) pay, out of and as part of the Aggregate Initial Cash Purchase Price, an aggregate of $185,000,000, such payment to be made by wire transfer of immediately available funds to a single bank account that shall be designated by notice given not less than three
business days before the Closing by the Company to Parent and signed by or on behalf of all the Company Unitholders. It is understood and agreed that such payment shall be applied, as the Company Unitholders shall determine, so as to satisfy any obligations of the Company and/or expenses of the Company relating to the Transactions, as further provided by the last sentence of Section 5.1, and otherwise shall be divided among the Company Unitholders ratably in accordance with their respective Target Percentage Interests pertaining to their Company Units. Parent, however, shall have no responsibility with respect to the application of such payment once made to such account; the Company and the Company Unitholders shall be responsible for satisfying at or before the Closing the obligations and expenses of the Company referred to in the last sentence of Section 5.1. The Acquiring Corp. on the third anniversary of the Closing Date (or, if such day is not a business day, the next business day) shall pay to the Company Unitholders, divided among them ratably in accordance with their respective Target Percentage Interests pertaining to their Company Units (as held immediately before the Closing as contemplated by Section 2.1(a)), the sum (the “Deferred Payment”) of (1) an aggregate of $25,000,000, out of and as part of the Aggregate Initial Cash Purchase Price, plus (2) the aggregate amount equal to the interest that would accrue on $25,000,000 at the Magellan Cash Investment Rate (or as provided below, at double such rate) on a daily basis, compounding quarterly, from the Closing Date to the date preceding the date of payment thereof, subject, however, to reduction of such amount (including the amount on which such interest accrual shall be calculated) if and as provided by Sections 2.1(g) and 5.10 or Article VIII. In the event that prior to the date the Deferred Payment becomes payable (1) the credit rating issued by Standard & Poors Corporation for Parent’s senior unsecured debt falls below a “B” rating or (2) the credit rating issued by Moody’s Investors Service for Parent’s senior unsecured debt falls below a “B2” rating or (3) Parent’s senior unsecured debt ceases to have any credit rating by Moody’s Investors Service or by Standard & Poors Corporation or (4) Parent receives a notice of default under its Credit Agreement, the Acquiring Corp. shall promptly after the happening of such event deposit into an escrow account to be established at Deutsche Bank Trust Company Americas. (the “Escrow Agent”) an amount of cash equal to the then amount of the Deferred Payment (including any portion thereof determined as an accrual of interest and after any reductions thereto theretofore made resulting from the application of Sections 2.1(g) or 5.10 or Article VIII) (the “Escrow Amount”) with the Escrow Agent to be held in an escrow account pursuant to an Escrow Agreement consistent with the terms of this Agreement and reasonably acceptable to Parent and the Unitholder Representative (the “Escrow Agreement”). In the event that the Escrow Amount is not so deposited into escrow by the Acquiring Corp. within 30 days after the happening of such event, the amount of the Deferred Payment shall increase by an amount equal to the interest that would accrue on the Deferred Payment at double the Magellan Cash Investment Rate on a daily basis, compounding quarterly, from the date following such thirtieth (30th) day to the date preceding the day the Deferred Payment Amount either is deposited in escrow as provided by the immediately preceding sentence or is paid to the Company Unitholders as provided hereby. The Escrow Amount shall be held in escrow pending resolution of claims for indemnification (if any) pursuant to Section 8.2 and may be reduced in respect of amounts payable as indemnification.
hereunder in accordance with Article VIII and may also be reduced as provided by Sections 2.1(g) or 5.10. The Escrow Amount shall be invested by the Escrow Agent in money-market instruments and interest thereon shall be added to and become part of the Escrow Amount. After such deposit in escrow, the Deferred Payment shall no longer increase by the amount equal to the accrual of interest at the Magellan Cash Investment Rate provided hereby but any earnings on the amount in escrow, after application to any income taxes due thereon and any expenses of the escrow, shall be for the benefit of the Company Unitholders. The Escrow Amount shall be paid to the Company Unitholders out of the escrow in accordance with the Escrow Agreement at the same time as the Deferred Payment would have been paid to the Company Unitholders. Notwithstanding the foregoing provisions of this Section 2.2(a), Parent may elect, in its discretion, in lieu of depositing the then Deferred Payment amount in escrow as provided by such provisions, to deliver to the Unitholder Representative an irrevocable letter of credit, issued by a bank reasonably acceptable to the Company and the Unitholder Representative, in the amount equal to the sum of (1) the then Deferred Payment amount at such time plus (2) the aggregate amount equal to the interest that would accrue on such amount on a daily basis, compounding quarterly, at the Magellan Cash Investment Rate in effect for the fiscal quarter of Parent immediately preceding such time over the period from the date to delivery of such letter of credit to the date on which the Deferred Payment is payable to the Company Unitholders hereunder. Such letter of credit shall permit the Unitholder Representative to draw thereon for the amount of the Deferred Payment on the date on which the Deferred Payment first becomes payable to the Company Unitholders hereunder and shall be in such customary form as Parent and the Unitholder Representative shall reasonably agree upon. For all purposes of this Agreement, references to the Escrow Amount shall also refer to such letter of credit if such letter of credit is delivered in lieu of depositing the Escrow Amount in escrow as provided above.

(b) Transfer Books; No Further Ownership Rights in Company Units. The Merger Consideration to be paid in respect of Company Units upon the surrender for exchange of Company Units in accordance with the terms of this Article II shall, as of the Effective Time, be in full satisfaction of all rights pertaining to such Company Units (or other securities, as applicable) previously represented by such Company Units, and as of the start of business on the day on which the Effective Time occurs, no further Transfers of Company Units shall be permitted (and the Company’s transfer books shall be closed) and there likewise shall be no further transfers by the Surviving Company of Company Units (or other securities of the Company, as applicable) that were outstanding immediately before the Effective Time. From and after the Effective Time, the holders of Company Units outstanding immediately before the Effective Time shall cease to have any rights with respect to such Company Units, except for the right to receive the Merger Consideration as provided herein or as otherwise specifically provided herein or by applicable law. If, at any time after the Effective Time, any certificate or instrument representing a Company Unit is presented to the Surviving Company for any reason, it shall be canceled.
(c) **No Liability for Abandoned Property.** Notwithstanding any provision of this Agreement to the contrary, none of the parties hereto or the Surviving company shall be liable to any Person for any consideration otherwise payable hereunder but delivered to a public official pursuant to any applicable abandoned property, escheat or similar Law.

(d) **Withholding Taxes.** Acquiring Corp. shall be entitled to deduct and withhold from any payment to be made to a Company Unitholder hereunder, other than a payment of the Aggregate Initial Cash Purchase Price, such amounts as may be required to be deducted and withheld by Acquiring Corp. (or Parent on its behalf) with respect to the making of such payment under the Internal Revenue Code of 1986, as amended, and the rules and regulations promulgated thereunder (the “Code”), or under any provision of state, local or foreign tax Law. To the extent amounts are so withheld and paid over to the appropriate taxing authority, the withheld amounts shall be treated for all purposes of this Agreement as having been paid to the Person in respect of which such deduction and withholding was made.

SECTION 2.3 **Adjustments to Company Units.** Notwithstanding any provision of this Article II to the contrary (but without in any way limiting the covenants in Section 5.2), if between the date of this Agreement and the Effective Time the outstanding number of Company Units shall have been changed into a different number of units or a different class of membership interest or other securities issued by the Company by reason of the occurrence of or record date for any dividend, subdivision, split, combination, reclassification, recapitalization, reorganization, exchange of membership interests or similar transaction, the consideration payable in respect of a Company Unit and any such changed or additional membership interests or securities of the Company as a result of the Merger shall be appropriately adjusted to reflect such dividend, subdivision, reclassification, recapitalization, split, combination, exchange of membership interests or similar transaction but no change shall be made in the aggregate Merger Consideration.

SECTION 2.4 **Guarantee of Parent.** The obligations of Acquiring Corp. to pay and deliver the Merger Consideration (including Parent Shares) to the Company Unitholders as herein provided is hereby unconditionally and irrevocably guaranteed by Parent. Parent’s guarantee herein shall be a guaranty of payment (and not of collection). Parent’s obligations hereunder as guarantor shall be no greater than those of the Acquiring Corp. and to the extent that the Acquiring Corp. is afforded conditions to its obligations, defenses, offsets, cure periods, notice periods, remedies and rights under this Agreement or applicable Law, Parent shall be entitled to the benefit of the same.

**ARTICLE III**

**Representations and Warranties of the Company**

The Company represents and warrants to Parent and Merger Sub that, except as set forth in the disclosure schedules (with specific reference to the Section or subsection of this Agreement to which the information stated in such disclosure relates)
SECTION 3.1 Organization, Standing and Corporate Power.

(a) The Company is a limited liability company duly organized, validly existing and in good standing under the Laws of the State of Delaware and Oncore Healthcare, LLC ("Oncore") is its only Subsidiary and is a limited liability company duly organized, validly existing and in good standing under the LLC Act. Each of the Company and Oncore has all requisite power and authority necessary for it as a limited liability company to own or lease all of its properties and assets and to carry on its business as it is now being conducted and as currently proposed by its management to be conducted. Each of the Company and its Subsidiaries is duly licensed or qualified to do business and is in good standing in each jurisdiction in which the nature of the business conducted by it or the character or location of the properties and assets owned or leased by it makes such licensing or qualification necessary.

(b) All the outstanding membership interests in Oncore have been duly authorized and validly issued and are fully paid and nonassessable and are owned by the Company free and clear of all liens, pledges, charges, mortgages, encumbrances, adverse rights or claims and security interests of any kind or nature whatsoever (including any restriction on the right to vote or transfer the same, except for such transfer restrictions of general applicability as may be provided under the Securities Act of 1933, as amended, and the rules and regulations promulgated thereunder (the “Securities Act”), or the “blue sky” laws of the various States of the United States) (collectively, “Liens”). Except as disclosed in Section 3.1(b) of the Company Disclosure Schedule, the Company does not own, directly or indirectly, any capital stock, voting securities or equity interests in any Person.

(c) The Company has delivered to Parent correct and complete copies of its certificate of formation and limited liability company agreement (the “Company Charter Documents”) and correct and complete copies of the certificate of formation and limited liability company agreement of Oncore (the “Subsidiary Documents”), in each case as amended to the date of this Agreement. All such Company Charter Documents and Subsidiary Documents are in full force and effect and neither the Company nor any of its Subsidiaries is in violation of any of their respective provisions. The Company has made available to Parent and its representatives correct and complete copies of the minutes (or, in the case of minutes that have not yet been finalized, drafts thereof) of all meetings, consent or actions of the Company Unitholders and of the Manager of the Company held since inception of the Company in January, 2003, and comparable documents for Oncore.

SECTION 3.2 Capitalization.

(a) The only membership interests in the Company are the Company Units and no other equity interests in or securities of the Company have been authorized.
for issuance by the Company. At the date hereof, (1) 1,000 Company Units were issued and outstanding, (2) no Company Units were held by the Company in its treasury, and (3) no Company Units were reserved for issuance, or issuable, upon conversion of any other convertible or exchangeable security of the Company or any other option or similar right or instrument ("Convertible Securities"). All outstanding Company Units have been duly authorized and validly issued, all payments required to be made in consideration of the issuance thereof have been fully paid and the issuance thereof was free of preemptive rights. Included in Section 3.2(a) of the Company Disclosure Schedule is a correct and complete list of all holders of Company Units and each such holder holds all the Company Units listed as owned by it free of any Liens or participation or other interests therein. Except as set forth above in this Section 3.2(a) or disclosed in Schedule 3.1(b) of the Company Disclosure Schedule or as otherwise expressly permitted by Section 5.1(b), no member interests, shares of capital stock, voting securities or equity interests in or of the Company or any Subsidiary are issued and outstanding nor are any subscriptions, options, warrants, calls, convertible or exchangeable securities, rights, commitments or agreements of any character providing for the issuance of any member interests, shares of capital stock, voting securities or equity interests in or of the Company or any Subsidiary.

(b) There are no outstanding obligations of the Company or any of its Subsidiaries to repurchase, redeem or otherwise acquire any member interests, shares of capital stock, voting securities or equity interests (or any options, warrants or other rights to acquire any member interests, shares of capital stock, voting securities or equity interests) of the Company or any of its Subsidiaries.

SECTION 3.3 Authority; Noncontravention; Voting Requirements.

(a) The Company has all necessary power and authority to execute and deliver this Agreement and to perform its obligations hereunder and to consummate the Merger and the other Transactions. The execution, delivery and performance by the Company of this Agreement, and the consummation by it of the Merger and the other Transactions, have been duly authorized and approved by its Manager, which has recommended to the Company Unitholders the approval of the Merger and this Agreement as in the best interests of the Company and the Company Unitholders, and by any vote, approval or consent required to be received from the Company Unitholders or the holders of any member interests, shares of capital stock, securities or equity interests in or of the Company or any Subsidiary of the Company (the "Unitholder Approval"). The Unitholder Approval includes any vote, consent or approval required in order (1) for the Company under the LLC Act and the Company Charter Documents and (2) for any Subsidiary of the Company under any Law under which such Subsidiary is organized and any Subsidiary Document and (3) for the Company and any Subsidiary of the Company under any agreement with any Company Unitholder or holder of any member interest, share of capital stock, security or equity interest in or of the Company or any Subsidiary to enter into and perform this Agreement, including to consummate the Merger and the other Transactions. The Unitholder Approval remains in full force and effect. All holders of Company Units have voted to approve this Agreement and the Merger and given any other consent or approval to this Agreement and the Merger which they are
entitled to give. No other action on the part of the Company is necessary to authorize the execution, delivery and performance by the Company of this
Agreement and the consummation by it of the Merger and the other Transactions. This Agreement has been duly executed and delivered by the Company
and, assuming due authorization, execution and delivery hereof by the other parties hereto, constitutes a legal, valid and binding obligation of the Company,
 enforceable against the Company in accordance with its terms, except that such enforceability (i) may be limited by bankruptcy, insolvency, fraudulent
transfer, reorganization, moratorium and other similar laws of general application affecting or relating to the enforcement of creditors’ rights generally and
(ii) is subject to general principles of equity, whether considered in a proceeding at law or in equity (the “Bankruptcy and Equity Exception”).

(b) Neither the execution and delivery of this Agreement by the Company nor the consummation by the Company of the Transactions,
nor compliance by the Company with any of the terms or provisions hereof, will (i) conflict with or violate any provision of the Company Charter Documents
or any of the Subsidiary Documents or (ii) assuming that the authorizations, consents and approvals referred to in Section 3.4 are obtained and the filings
referred to in Section 3.4 are made, violate any Law, judgment, writ or injunction or Permit of any Governmental Authority or any arbitration award
applicable to the Company or any of its Subsidiaries or any of their respective properties or assets, or (iii) assuming that the authorizations, consents and
approvals described in Section 3.3(b) of the Company Disclosure Schedules are obtained and the filings disclosed in said Schedule are made, violate, conflict
with, result in the loss of any benefit under, constitute a default (or an event which, with notice or lapse of time, or both, would constitute a default) under,
result in the termination of or a right of termination or cancellation of, accelerate the performance required by, or result in the creation of any Lien upon any
of the respective properties or assets of the Company or any of its Subsidiaries under, any of the terms, conditions or provisions of any loan or credit
agreement, debenture, note, bond, mortgage, indenture, deed of trust, license, lease, insurance policy, contract or other agreement, instrument or obligation
(each, a “Contract”) or Permit, to which the Company or any of its Subsidiaries is a party, or by which it or any of its properties or assets may be bound or
affected. Without limiting the generality of the immediately preceding sentence, the Company does not have any unsatisfied obligation under any Contract
to notify any Person of the Company entering into, or having intended to enter into, this Agreement before doing so or to negotiate with any Person
regarding a possible alternative to the Transactions.

(c) Each of the persons identified in Section 3.3(c) of the Company Disclosure Schedules have entered into a Subscription Agreement
with Parent, which is effective as of the date hereof, providing for the purchase by it of certain Parent Shares simultaneously with the Closing and governing
the terms on which such Parent Shares shall be held and in the form approved by Parent (collectively, the “Subscription Agreements”).

SECTION 3.4 Governmental Approvals. Except for (1) the filing of the Certificate of Merger with the Secretary of State of the State of
Delaware pursuant to the
DGCL and the LLC Act, (2) filings required under, and compliance with other applicable requirements of, the HSR Act and (3) as described on Section 3.4 of the Company Disclosure Schedule, no consents or approvals of, or filings, declarations or registrations with, any Governmental Authority (each, a “Governmental Approval”) are necessary for the execution, delivery and performance of this Agreement by the Company and the consummation by the Company of the Transactions.

SECTION 3.5 Financial Statements and Controls

(a) The Company has delivered to Parent copies of (i) the audited consolidated balance sheets of the Company and the Subsidiaries as at December 31, 2004 and 2003 and the related audited consolidated statements of income and of cash flows of the Company and the Subsidiaries for the years then ended, and related audit reports of Regan, Russell, Schickner & Shah, LLC, and also, the audited consolidated balance sheet as at December 31, 2005 of the Company and Subsidiaries and the related audited consolidated statements of income and of cash flows for the year then ended, and the related audit report of Mayer Hoffman McCann, P.C., (ii) the unaudited consolidated balance sheet of the Company and the Subsidiaries as at March 31, 2006 and the related consolidated statements of income and cash flows of the Company and the Subsidiaries for the three month period then ended (such audited and unaudited statements, including the related notes and schedules thereto, are referred to herein as the “Financial Statements”). Each of the Financial Statements is complete and correct in all material respects, has been prepared in accordance with GAAP consistently applied by the Company without modification of the accounting principles used in the preparation thereof throughout the periods presented (except as noted therein) and presents fairly in all material respects the consolidated financial position, results of operations and cash flows of the Company and the Subsidiaries as at the dates and for the periods indicated therein subject in the case of the unaudited statements to the absence of footnotes and other supplemental information that would be required by GAAP and to normal year-end audit adjustments. The consolidated balance sheet of the Company and the Subsidiaries as at December 31, 2005 audited by Mayer Hoffman McCann, P.C. is referred to herein as the “Balance Sheet” and December 31, 2005 is referred to herein as the “Balance Sheet Date”.

(b) All books, records and accounts of the Company and the Subsidiaries are accurate and complete and are maintained in all material respects in accordance with good business practice and all applicable Laws. The Company and the Subsidiaries maintain systems of internal accounting controls sufficient to provide reasonable assurances that: (i) transactions are executed in accordance with management’s general or specific authorization; (ii) transactions are recorded as necessary to permit the preparation of financial statements in conformity with GAAP and to maintain accountability for assets; (iii) access to assets is permitted only in accordance with management’s general or specific authorization; and (iv) the recorded accountability for assets is compared with the actual levels at reasonable intervals and appropriate action is taken with respect to any differences.
(c) The financial projections and business plan provided by the Company to Parent prior to the date hereof were reasonably prepared on a basis reflecting management’s best estimates, assumptions and judgments, at the time prepared, as to the future financial performance of the Company and the Subsidiaries.

(d) Each of the Company’s principal executive officer and its principal financial officer have disclosed to the auditors that have prepared the audited financial statements referred to in Section 3.5(a) the existence at any time since the commencement of business by the Company and its Subsidiaries, to their Knowledge, of (i) any significant deficiency in the design or operation of the Company’s internal control over financial reporting (as defined in Rule 13a-15 under the Exchange Act) and (ii) the occurrence since such date of any fraud, whether or not material, that involves management or other employees who have a significant role in the Company’s internal control over financial reporting.

SECTION 3.6 No Undisclosed Liabilities

(a) Neither the Company nor any Subsidiary has any indebtedness or Liabilities other than those (i) fully reflected on or reserved against in the Balance Sheet or, if not required under GAAP to be reflected on a balance sheet, disclosed in the notes thereto or pursuant to another representation or warranty of the Company contained in this Article or the Company Disclosure Schedule or (ii) incurred after the Balance Sheet Date in the ordinary course of business consistent with past practice.

(b) Neither the Company nor any of its Subsidiaries is a party to, or has any commitment to become a party to, any joint venture, off-balance sheet partnership or any similar Contract (including any Contract or arrangement relating to any transaction or relationship between or among the Company and any of its Subsidiaries, on the one hand, and any unconsolidated Affiliate, including any structured finance, special purpose or limited purpose entity or Person, on the other hand, or any “off-balance sheet arrangements” (as defined in Item 303(a) of Regulation S-K of the SEC)), where the result, purpose or effect of such Contract is to avoid disclosure of any transaction involving, or liabilities of, the Company or any of its Subsidiaries in the Company’s or such Subsidiary’s financial statements.

SECTION 3.7 Absence of Certain Changes or Events. Since the Balance Sheet Date there have not been any events, changes in circumstances or states of facts that, individually or in the aggregate, have had or could reasonably be expected to have a Material Adverse Effect on the Company. Since the Balance Sheet Date (a) the Company and its Subsidiaries have carried on and operated their respective businesses in the ordinary course of business consistent with past practice and (b) neither the Company nor any of its Subsidiaries has taken any action described in Section 5.2 hereof that if taken after the date hereof and prior to the Effective Time without the prior written consent of Parent would violate such provision. Without limiting the foregoing, since the Balance Sheet Date there has not occurred any damage, destruction or loss (whether or
not covered by insurance) of any material asset of the Company or any of its Subsidiaries which materially affects the use thereof.

SECTION 3.8 Legal Proceedings. There is no pending or, to the Knowledge of the Company, threatened, legal, administrative, arbitral or other proceeding, claim, suit or action against, or governmental or regulatory investigation of, or healthcare regulatory review proceedings involving, the Company or any of its Subsidiaries, nor is there any injunction, order, judgment, ruling or decree imposed (or, to the Knowledge of the Company, threatened to be imposed) upon the Company, any of its Subsidiaries or the assets of the Company or any of its Subsidiaries, by or before any Governmental Authority or arbitrator, (a) including any of the foregoing that challenges any of the Transactions, provided that the representation in clause (a) is made only as of the date hereof.

SECTION 3.9 Compliance With Laws. The Company and its Subsidiaries are (and since their commencement of business have been) in compliance with all laws (including common law), statutes, ordinances, codes, rules, regulations, decrees and orders of Governmental Authorities (collectively, “Laws”) applicable to the Company or any of its Subsidiaries, any of their properties or other assets or any of their businesses or operations. Since their commencement of business, neither the Company nor any of its Subsidiaries has received written notice to the effect that a Governmental Authority claimed or alleged that the Company or any of its Subsidiaries was not in compliance with all Laws applicable to the Company or any of its Subsidiaries, any of their properties or other assets or any of their businesses or operations.

SECTION 3.10 Taxes.

(a) Each of the Company and its Subsidiaries has timely filed, or has caused to be timely filed on its behalf (taking into account any extension of time within which to file), all Tax Returns required to be filed by it, and all such filed Tax Returns are correct and complete. All Taxes shown to be due on such Tax Returns, or otherwise required to be paid by the Company or any of its Subsidiaries, have been timely paid. The Company has complied with all applicable Laws relating to the payment and/or withholding of such Taxes, and has timely withheld and paid over to the appropriate Governmental Authority all amounts required to be so withheld and paid under all applicable Laws.

(b) Neither the Company nor any of its Subsidiaries has been a member of an affiliated group of corporations within the meaning of Section 1504 of the Code, other than the affiliated group of which the Company is the common parent.

(c) Neither the Company nor its Subsidiaries has any outstanding agreements, waivers, or arrangements extending the statutory period of limitations applicable to any claim for, or the period for the collection or assessment of Taxes. No claim has been made by a taxing authority in a jurisdiction where the Company or any of its Subsidiaries does not file Tax Returns that the Company or such Subsidiary of the
Company is or may be subject to taxation in that jurisdiction. No Liens for Taxes exist with respect to any assets or properties of the Company or any of its Subsidiaries, except for Liens for Taxes not yet due.

(d) The Tax Returns of the Company and its Subsidiaries have never been examined.

(e) No audit or other administrative or court proceedings are pending with any Governmental Authority with respect to Taxes of the Company or any of its Subsidiaries and no notice thereof has been received.

(f) The Company has made available to Parent correct and complete copies of (i) all income and other material Tax Returns of the Company and its Subsidiaries for the preceding three taxable years and (ii) any audit report issued within the last three years (or otherwise with respect to any audit or proceeding in progress) relating to Taxes of the Company or any of its Subsidiaries.

(g) Neither the Company nor any of its Subsidiaries will be required to include any item of income in, or exclude any deduction in calculating, taxable income for any taxable period (or portion thereof) ending after the Closing Date as a result of any: (i) change in method of accounting for a taxable period ending on or prior to the Closing Date; (ii) “closing agreement” as described in Section 7121 of the Code (or any corresponding or similar provision of state, local or foreign Tax law) executed on or prior to the Closing Date; or (iii) installment sale or open transaction disposition made on or prior to the Closing Date;

(h) Neither the Company nor any of its Subsidiaries is or has been a “United States real property holding corporation” within the meaning of Section 897 of the Code during the five-year period ending on the Closing Date.

(i) No property owned by the Company or any Subsidiary is (1) property required to be treated as being owned by another Person pursuant to the provisions of Section 168(f)(8) of the Internal Revenue Code of 1954, as amended and in effect immediately prior to the enactment of the Tax Reform Act of 1986, (2) “tax-exempt use property” within the meaning of Section 168(h)(1) of the Code, (3) “tax-exempt bond financed property” within the meaning of Section 168(g) of the Code, (4) subject to Section 168(g)(1) of the Code, (5) “limited use property” within the meaning of Rev. Proc. 2001-28, or (6) subject to any provision of state, local or foreign law comparable to any of the preceding provisions.

(j) Neither the Company nor any Subsidiary is a party to any tax sharing, allocation, indemnity or similar agreement or arrangement (whether or not written) pursuant to which such entity will have any obligation to make any payments after the Closing.
Neither the Company nor any Subsidiary is the subject of any private letter ruling of the Internal Revenue Service or comparable rulings of other Governmental Authorities.

Neither the Company nor any Subsidiary has a permanent establishment in any country other than the United States, and is not subject to tax in a jurisdiction outside the United States.

Neither the Company nor any of its Subsidiaries has filed any election in any jurisdiction to be taxed as a corporation and is and has always been treated as a partnership by all Governmental Authorities in which it is obligated either to pay Tax or file a Tax Return. No member in the Company or any of its Subsidiaries has filed a Form 8082 (or similar form or statement for U.S. federal, state, local or foreign income Tax purposes) notifying the applicable Governmental Authority of an inconsistent treatment of an item on the Company’s or any of its Subsidiaries’ Tax Returns.

The Company and its Subsidiaries have disclosed on its Tax Returns all positions taken therein that could give rise to a substantial understatement of federal income tax within the meaning of Section 6662 of the Code (or any corresponding local law).

Neither the Company nor any of its Subsidiaries has engaged in any “reportable transactions” as defined in Treasury Regulation Section 1.6011-4(b).

For purposes of this Agreement: (x) “Taxes” shall mean (A) all federal, state, local or foreign taxes, charges, fees, imposts, levies or other assessments, including all net income, gross receipts, capital, sales, use, ad valorem, value added, transfer, franchise, profits, inventory, capital stock, license, withholding, payroll, employment, social security, unemployment, excise, severance, stamp, occupation, property and estimated taxes, customs duties, fees, assessments and charges of any kind whatsoever, (B) all interest, penalties, fines, additions to tax or additional amounts imposed by any Governmental Authority in connection with any item described in clause (A), and (C) any liability in respect of any items described in clauses (A) or (B) payable by reason of contract, assumption, transferee liability, operation of Law, Treasury Regulation Section 1.1502-6(a) (or any predecessor or successor thereof of any analogous or similar provision under Law) or otherwise, and (y) “Tax Returns” shall mean any return, report, claim for refund, estimate, information return or statement or other similar document relating to or required to be filed or actually filed with any Governmental Authority with respect to Taxes, including any schedule or attachment thereto, and including any amendment thereof.

SECTION 3.11 Employee Benefits and Labor Matters

Section 3.11(a) of the Company Disclosure Schedule sets forth a correct and complete list of: (i) all full- or part-time employment, consulting, sales commission or similar compensatory agreements, (ii) all “employee benefit plans” (as
defined in Section 3(3) of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), (iii) all bonus or other incentive compensation, stock purchase, equity or equity-based compensation plans, policies, agreements or arrangements, (iv) all severance, change in control, deferred compensation or loan plans, policies, agreements or arrangements, (v) all health insurance or benefit, life insurance, disability insurance, salary continuation or educational assistance plans, policies, agreements or arrangements, (vi) all material payroll practices, including sick leave and vacation policies, programs or arrangements and (vii) all other material employee benefit plans, policies, agreements or arrangements, in each case with respect to which the Company or any of its Subsidiaries has any obligation or liability, contingent or otherwise, for current or former employees, consultants, managers or directors of the Company or any of its Subsidiaries (collectively, the "Company Plans"). Section 3.11(a) of the Company Disclosure Schedule separately sets forth each Company Plan which is subject to Title IV of ERISA or is a “multiemployer plan”, as defined in Section 3(37) of ERISA (a “Multiemployer Plan”), or is or has been subject to Sections 4063 or 4064 of ERISA.

(b) Correct and complete copies of the following documents with respect to each of the Company Plans (other than a Multiemployer Plan) have been delivered to Parent by the Company to the extent applicable: (i) any plans and related trust documents, insurance contracts or other funding arrangements, and all amendments thereto; (ii) the most recent Forms 5500 and all schedules thereto, (iii) the most recent actuarial report, if any; (iv) the most recent IRS determination letter; (v) the most recent summary plan descriptions; and (vi) written summaries of all non-written Company Plans.

(c) The Company Plans have been maintained in accordance with their terms and with all applicable provisions of ERISA, the Code and other Laws.

(d) The Company Plans intended to qualify under Section 401 or other tax-favored treatment under of Subchapter B of Chapter 1 of Subtitle A of the Code are so qualified, and any trusts intended to be exempt from federal income taxation under the Code are so exempt. Nothing has occurred with respect to the operation of the Company Plans that could cause the loss of such qualification or exemption, or the imposition of any liability, penalty or tax under ERISA or the Code.

(e) Parent will not have any obligation to make any contribution or other payment to any Multiemployer Plan which it would not have had but for the consummation of the transactions.

(f) All contributions required to have been made under any of the Company Plans or by law (without regard to any waivers granted under Section 412 of the Code), have been timely made, and no accumulated funding deficiencies exist in any of the Company Plans subject to Title IV of ERISA or Section 412 of the Code.

(g) The “benefit liabilities” as defined in Section 4001(a)(16) of ERISA of each Title IV Plan using the actuarial assumptions used by the Pension Benefit...
Guaranty Corporation ("PBGC") to determine the level of funding required in the event of the termination of such Title IV Plan do not exceed the assets of such Title IV Plan.

(h) There are no pending actions, claims or lawsuits arising from or relating to the Company Plans, (other than routine benefit claims), nor does the Company have any Knowledge of facts that could form the basis for any such claim or lawsuit.

(i) All amendments and actions required to bring the Company Plans into conformity with all of the applicable provisions of the Code, ERISA and other applicable Laws have been made or taken, except to the extent that such amendments or actions are not required by law to be made or taken until a date after the Closing Date and, to the knowledge of the Company, are described on Section 3.11(i) of the Company Disclosure Schedule.

(j) None of the Company Plans provide for post-employment life or health coverage for any participant or any beneficiary of a participant, except as may be required under Part 6 of the Subtitle B of Title I of ERISA and at the expense of the participant or the participant’s beneficiary.

(k) Neither the execution and delivery of this Agreement nor the consummation of the Transactions will (i) result in any payment becoming due to any employee, (ii) increase any benefits otherwise payable under any Company Plan, (iii) result in the acceleration of the time of payment or vesting of any such benefits under any such plan, or (iv) require any contributions or payments to fund any obligations under any Company Plan.

(l) Any individual who performs services for the Company or any of its Subsidiaries (other than through a contract with an organization other than such individual) and who is not treated as an employee of the Company or any of its Subsidiaries for federal income tax purposes by the Company is not an employee for such purposes.

(m) None of the employees of the Company or its Subsidiaries is represented in his or her capacity as an employee of the Company or any of its Subsidiaries by any labor organization. Neither the Company nor any of its Subsidiaries has recognized any labor organization, nor has any labor organization been elected as the collective bargaining agent of any employees, nor has the Company or any of its Subsidiaries entered into any collective bargaining agreement or union contract recognizing any labor organization as the bargaining agent of any employees. There is no union organization activity involving any of the employees of the Company or any of its Subsidiaries pending or, to the Knowledge of the Company, threatened, nor has there ever been union representation involving any of the employees of the Company or any of its Subsidiaries. There is no picketing pending or, to the Knowledge of the Company, threatened, and there are no strikes, slowdowns, work stoppages, other job actions, lockouts, arbitrations, grievances or other labor disputes involving any of the employees of the Company or any of its Subsidiaries pending or, to the Knowledge of the Company,
threatened. There are no complaints, charges or claims against the Company or any of its Subsidiaries pending or, to the Knowledge of the Company, threatened that could be brought or filed with any Governmental Authority or arbitrator based on, arising out of, in connection with, or otherwise relating to the employment or termination of employment or failure to employ by the Company or any of its Subsidiaries, of any individual. The Company and its Subsidiaries are in compliance with all Laws relating to the employment of labor, including all such Laws relating to wages, hours, the Worker Adjustment and Retraining Notification Act and any similar state or local “mass layoff” or “plant closing” law (“WARN”), collective bargaining, discrimination, civil rights, safety and health, workers’ compensation and the collection and payment of withholding and/or social security taxes and any similar tax. There has been no “mass layoff” or “plant closing” (as defined by WARN) with respect to the Company or any of its Subsidiaries since January 1, 2005.

SECTION 3.12 Environmental Matters

(a) (A) each of the Company and its Subsidiaries is, and has been, in compliance with all applicable Environmental Laws, (B) there is no investigation, suit, claim, action or proceeding relating to or arising under Environmental Laws that is pending or, to the Knowledge of the Company, threatened against or affecting the Company or any of its Subsidiaries or any real property currently or, to the Knowledge of the Company, formerly owned, operated or leased by the Company or any of its Subsidiaries, (C) neither the Company nor any of its Subsidiaries has received any notice of or entered into or assumed by Contract or operation of Law or otherwise, any obligation, liability, order, settlement, judgment, injunction or decree relating to or arising under Environmental Laws, and (D) no facts, circumstances or conditions exist with respect to the Company or any of its Subsidiaries or any property currently (or, to the Knowledge of the Company, formerly) owned, operated or leased by the Company or any of its Subsidiaries or any property to or at which the Company or any of its Subsidiaries transported or arranged for the disposal or treatment of Hazardous Materials that could reasonably be expected to result in the Company and its Subsidiaries incurring Environmental Liabilities. The Company has provided to Parent correct and complete copies of all existing environmental reports, reviews and audits and all written information pertaining to actual or potential Environmental Liabilities relating to the Company or its Subsidiaries.

(b) For purposes of this Agreement:


24

(ii) “Environmental Liabilities” means, with respect to any Person, all liabilities, obligations, responsibilities, remedial actions, losses, damages, punitive damages, consequential damages, treble damages, costs and expenses (including all reasonable fees, disbursements and expenses of counsel, experts and consultants and costs of investigation and feasibility studies), fines, penalties, sanctions and interest incurred as a result of any claim or demand by any other Person or in response to any violation of Environmental Law, whether known or unknown, accrued or contingent, whether based in contract, tort, implied or express warranty, strict liability, criminal or civil statute, to the extent based upon, related to, or arising under or pursuant to any Environmental Law, environmental permit, order or agreement with any Governmental Authority or other Person, which relates to any environmental, health or safety condition, violation of Environmental Law or a Release or threatened Release of Hazardous Materials.

(iii) “Hazardous Materials” means any material, substance of waste that is regulated, classified, or otherwise characterized under or pursuant to any Environmental Law as “hazardous”, “toxic”, a “pollutant”, a “contaminant”, “radioactive” or words of similar meaning or effect, including petroleum and its by-products, asbestos, polychlorinated biphenyls, radon, mold, urea formaldehyde insulation, chlorofluorocarbons and all other ozone-depleting substances.

(iv) “Release” means any spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, dumping, disposing of or migrating into or through the environment or any natural or man-made structure.

SECTION 3.13 Contracts.

(a) Set forth in Section 3.13(a) of the Company Disclosure Schedules is a list of each Contract of the following types or having the following terms to which the Company or any of its Subsidiaries is a party:

(i) a Contract that purports to limit, curtail or restrict the ability of the Company or any of its existing or future Subsidiaries or Affiliates or any of its Company Unitholders to compete in any geographic area or line of
business or restrict the Persons to whom the Company or any of its existing or future Subsidiaries or Affiliates may sell products or deliver services;

(ii) a partnership or joint venture agreement;

(iii) a Contract for the acquisition, sale or lease of properties or assets (by merger, purchase or sale of stock or assets or otherwise) entered into since their commencement of business;

(iv) a Contract with any (x) Governmental Authority or (y) manager, director or officer of the Company or any of its Subsidiaries or any Affiliate of the Company;

(v) a loan or credit agreement, mortgage, indenture, note or other Contract or instrument evidencing indebtedness for borrowed money by the Company or any of its Subsidiaries or any Contract or instrument pursuant to which indebtedness for borrowed money may be incurred or is guaranteed by the Company or any of its Subsidiaries;

(vi) a financial derivatives master agreement or confirmation, or futures account opening agreements and/or brokerage statements, evidencing financial hedging or similar trading activities;

(vii) an agreement relating to the transfer or voting of, or providing for registration rights with respect to, member interests, shares of capital stock, securities or equity interests in or of the Company or any Subsidiary;

(viii) a mortgage, pledge, security agreement, deed of trust, hypothecation, or other Contract granting a Lien on any property or assets of the Company or any of its Subsidiaries;

(ix) a customer or client Contract;

(x) a Contract (other than one with a customer or client) that involves consideration (whether or not measured in cash) of greater than $10,000 or has a duration extending beyond December 31, 2006 unless it may be terminated by the Company without penalty on not more than 90 days notice;

(xi) a collective bargaining agreement;

(xii) a “standstill” or similar agreement;

(xiii) a Contract for the employment of any individual on a full-time or part-time basis;

(xiv) a Contract providing for severance, retention, change in control or similar payments;
(xv) Contracts relating to employee options;

(xvi) to the extent material to the business or financial condition of the Company and its Subsidiaries, taken as a whole, any (1) lease or rental Contract, (2) product design or development Contract, (3) consulting Contract, (4) indemnification Contract, (5) license or royalty Contract, or (6) merchandising, sales representative or distribution Contract;

(xvii) Contracts granting a right of first refusal or first negotiation; and

(xviii) commitments or agreements to enter into any of the foregoing.

In addition, no Company Unitholder is a party to or is bound by any agreement or other obligation which prevents it from providing the services he currently provides to the Company or that are contemplated to be provided by him after the Closing pursuant to his Employment Agreement referred to in Section 3.25. Each of the Contracts and other documents required to be listed on Section 3.13(a) of the Company Disclosure Schedule, together with any and all other Contracts of such type entered into in accordance with Section 5.2 is a “Material Contract.” The Company has heretofore made available to Parent correct and complete copies of each Material Contract in existence as of the date hereof, together with any and all amendments and supplements thereto and material “side letters” and similar documentation relating thereto.

(b) Each of the Material Contracts is valid, binding and in full force and effect and is enforceable in accordance with its terms by the Company and its Subsidiaries party thereto, subject to the Bankruptcy and Equity Exception. Section 3.13(b) of the Company Disclosure Schedules sets forth an accurate and complete list of all Contracts between the Company and/or its Subsidiaries and customers or clients of the Company and/or its Subsidiaries which contain provisions that would give rise to a right of termination by such customer or client as a result of the entry into this Agreement or the consummation of the Transactions, i.e., as a result of change in control provisions (the “Change In Control Customer Contracts”). Except as identified in Section 3.13(b) of the Company Disclosure Schedule, no approval, consent or waiver of, or notice to, any Person is needed in order that any Material Contract (including any Change In Control Customer Contract) to continue in full force and effect following the consummation of the Transactions. Neither the Company nor any of its Subsidiaries is in default under any Material Contract or other Contract to which the Company or any of its Subsidiaries is a party (collectively, the “Company Contracts”), nor does any condition exist that, with notice or lapse of time or both, would constitute a default thereunder by the Company and its Subsidiaries party thereto. To the Knowledge of the Company, no other party to any Company Contract is in default thereunder, nor does any condition exist that with notice or lapse of time or both would constitute a default by any such other party thereunder. Neither the Company nor any of its Subsidiaries has received any notice of termination or cancellation under any Material Contract, received any notice of breach or default under
any Material Contract which breach has not been cured, or granted to any third party any rights, adverse or otherwise, that would constitute a breach of any Material Contract.

(c) Except as set forth in Section 3.13(c) of the Company Disclosure Schedules, since the Balance Sheet Date, no customer or client identified on Section 3.13(a) of the Company Disclosure Schedule pursuant to clause (ix) thereof has terminated its relationship with the Company or materially reduced or changed the pricing or other terms of its business with the Company and, to the Knowledge of the Company, no such customer has notified the Company in writing that it intends to terminate or materially reduce or change the pricing or other terms of its business with the Company.

(d) The Company has satisfied all performance standards under any Material Contract where it is required to do so in order to receive any fees, bonuses, rebates, incentives, or other payments at the levels at which it has received fees or payments under such Contract in the last or the current fiscal year and is not required to return any fees or payments received by it or to provide credits against any future fees or payment that would otherwise be due to it under any Contract, nor is it subject to any penalties under any such Contract, by reason of its failure to satisfy any performance standard contained in such Contract.

SECTION 3.14 Title to Properties. Each of the Company and its Subsidiaries (i) has good and valid title to all real properties and all other material properties which are reflected on the most recent consolidated balance sheet of the Company as being owned by the Company or one of its Subsidiaries (or acquired after the date thereof) (except properties sold or otherwise disposed of since the date thereof in the ordinary course of business consistent with past practice and not in violation of this Agreement), free and clear of all Liens except (x) statutory liens securing payments not yet due, (y) security interests, mortgages and pledges that secure indebtedness for borrowed money that is reflected in the most recent consolidated financial statements of the Company and (z) such other imperfections or irregularities of title or other Liens that, individually or in the aggregate, do not and would not reasonably be expected to materially affect the use of the properties or assets subject thereto or otherwise materially impair business operations as presently conducted or as currently proposed by the Company’s management to be conducted (any Lien described in (x), (y) or (z) above, a “Permitted Lien”), and (ii) is the lessee or sublessee of all leasehold estates and leasehold interests in all properties or assets which are used in the Company’s business and not owned by the Company as referred to in the foregoing clause (i). Each of the Company and its Subsidiaries enjoys peaceful and undisturbed possession under all such leases in all material respects.
SECTION 3.15  Intellectual Property.

(a) For purposes of this Agreement:

(i) “Company Intellectual Property” means all Intellectual Property Rights used in or necessary for the conduct of the business of the Company or any of its Subsidiaries, or owned or held for use by the Company or any of its Subsidiaries.

(ii) “Company Technology” means all Technology used in or necessary for the conduct of the business of the Company or any of its Subsidiaries, or owned or held for use by the Company or any of its Subsidiaries.

(iii) “Intellectual Property Rights” shall mean all of the rights arising from or in respect of the following, whether protected, created or arising under the Laws of the United States or any foreign jurisdiction: (A) patents, patent applications, any reissues, reexaminations, divisionals, continuations, continuations-in-part and extensions thereof (collectively, “Patents”); (B) trademarks, service marks, trade names (whether registered or unregistered), service names, industrial designs, brand names, brand marks, trade dress rights, Internet domain names, identifying symbols, logos, emblems, signs or insignia, and including all goodwill associated with the foregoing (collectively, “Marks”); (C) copyrights, whether registered or unregistered (including copyrights in computer software programs), mask work rights and registrations and applications therefor (collectively, “Copyrights”); (D) confidential and proprietary information, or non-public processes, designs, specifications, technology, know-how, techniques, formulas, inventions, concepts, trade secrets, discoveries, ideas and technical data and information, in each case excluding any rights in respect of any of the foregoing that comprise or are protected by Copyrights or Patents (collectively, “Trade Secrets”); and (E) all applications, registrations and permits related to any of the foregoing clauses (A) through (D).

(iv) “Publicly Available Software” means any open source or free Software (including any Software licensed pursuant to a GNU public license) or other Software that requires as a condition of use, modification or distribution that other Software incorporated into, derived from or distributed with such Software (a) be disclosed or distributed in source code form, (b) be licensed for the purpose of making derivative works or (c) be redistributable at no charge.

(v) “Software” means computer programs, including any and all software implementations of algorithms, models and methodologies whether in source code, object code or other form, databases and compilations, including any and all data and collections of data, descriptions, flow-charts and other documentation used in the ordinary course of business in the use thereof.
(vi) “Technology” means, collectively, all designs, formulas, algorithms, procedures, techniques, ideas, know-how, Software (whether in source code, object code or human readable form), databases and data collections, Internet websites and web content, tools, inventions (whether patentable or unpatentable and whether or not reduced to practice), invention disclosures, developments, creations, improvements, works of authorship, other similar materials and all recordings, graphs, drawings, reports, analyses, other writings and any other embodiment of the above, in any form or media, whether or not specifically listed herein.

(b) Section 3.15(b) of the Company Disclosure Schedule sets forth an accurate and complete list of all Patents, registered Marks, pending applications for registrations of any Marks and any unregistered Marks, registered Copyrights and pending applications for registration of any Copyrights, in each case, owned or filed by the Company or any of its Subsidiaries. Section 3.15(b) of the Company Disclosure Schedule lists the jurisdictions in which each such Intellectual Property right has been issued or registered or in which any application for such issuance and registration has been filed.

(c) The Company and/or one of its Subsidiaries is the sole and exclusive owner of, or has valid and continuing rights to use, sell and license, all of the Company Intellectual Property and Company Technology, in each case, owned or purported to be owned by or licensed to the Company or any of its Subsidiaries. The use, practice or other commercial exploitation of the Company Intellectual Property by the Company or any of its Subsidiaries and the manufacturing, licensing, marketing, importation, offer for sale, sale or use of the Company Technology, and the operation of the Company’s and its Subsidiaries’ businesses do not infringe, constitute an unauthorized use of, violate, or misappropriate any Intellectual Property Rights of any third Person. Neither the Company nor any of its Subsidiaries is a party to or the subject of any pending or, to the Knowledge of the Company, threatened suit, action, investigation or proceeding which involves a claim (A) against the Company or any of its Subsidiaries, of infringement, unauthorized use, or violation of any Intellectual Property Rights of any Person, or challenging the ownership, use, validity or enforceability of any Company Intellectual Property or (B) contesting the right of the Company or any of its Subsidiaries to use, sell, exercise, license, transfer or dispose of any Company Intellectual Property or Company Technology, or any products, processes or materials covered thereby in any manner. The Company has not received written notice of any such threatened claim nor to the Company’s Knowledge are there any facts or circumstances that would form the basis for any claim against the Company or any of its Subsidiaries of infringement, unauthorized use, or violation of any Intellectual Property Rights of any Person, or challenging the ownership, use, validity or enforceability of any Company Intellectual Property or Company Technology.

(d) To the Knowledge of the Company, no Person (including employees and former employees of the Company or any of its Subsidiaries) is infringing, violating, misappropriating or otherwise misusing any Company Intellectual
Property, and neither the Company nor any of its Subsidiaries has made any such claims against any Person (including employees and former employees of the Company or any of its Subsidiaries) nor, to the Knowledge of the Company, is there any basis for such a claim.

(c) No Trade Secret or any other non-public, proprietary information of the Company or any of its Subsidiaries as presently conducted has been authorized to be disclosed or has been actually disclosed by the Company or any of its Subsidiaries to any employee or any third Person other than pursuant to a confidentiality or non-disclosure agreement restricting the disclosure and use of the Company Intellectual Property or Company Technology. The Company and its Subsidiaries have taken all reasonably necessary and appropriate steps to protect and preserve the confidentiality of all Trade Secrets and any other non-public, proprietary or confidential information of the Company or its Subsidiaries.

(f) Section 3.15(f) of the Company Disclosure Schedule sets forth a correct and complete list of all Software that is (i) owned exclusively by the Company or any of its Subsidiaries; or (ii) used by the Company or its Subsidiaries in their businesses and not exclusively owned by the Company or its Subsidiaries or available on reasonable terms through commercial distributors or in consumer retail stores.

(g) Except as set forth in Section 3.15(g) of the Company Disclosure Schedule, no Publicly Available Software (including, without limitation, all derivative works thereof) (i) was used in connection with the development or modification of any Software used by the Company or any of its Subsidiaries, (ii) forms part of the Technology owned by the Company or any Subsidiary, (iii) is, in whole or in part, embodied or incorporated into any of the Company’s or any of its Subsidiaries’ products, or (iv) was or is used in connection with the development of any Technology owned by the Company or any Subsidiary or any of the Company’s or any of its Subsidiaries’ products.

(h) The Company and its Subsidiaries own, lease or license all Software, hardware, databases, computer equipment and other information technology (collectively, "Computer Systems") that are necessary for the operations of the Company’s and its Subsidiaries’ businesses. The Computer Systems used by the Company and its Subsidiaries have functioned consistently and accurately since being installed. The data storage and transmittal capability, functionality and performance of each item of the Computer Systems and the Computer Systems as a whole are adequate for the Company’s and its Subsidiaries’ businesses. The Computer Systems have not failed to any material extent and the data which they process has not been corrupted. The Company and its Subsidiaries have taken all reasonable steps in accordance with industry standards to preserve the availability, security and integrity of the Computer Systems and the data and information stored on the Computer Systems. The Company and its Subsidiaries maintain comprehensive and clear documentation regarding all Computer Systems, their methods of operation, and their support and maintenance.
Section 3.16 Insurance. Section 3.16 of the Company Disclosure Schedule sets forth a correct and complete summary of the material insurance policies held by, or for the benefit of, the Company and its Subsidiaries as of the date of this Agreement, including the underwriter of such policies and the amount of the coverage thereunder) maintained by the Company or any of its Subsidiaries (the “Policies”). The Policies (i) have been issued by insurers which, to the Knowledge of the Company, are reputable and financially sound, (ii) provide coverage for the operations conducted by the Company and its Subsidiaries of a scope and coverage consistent with customary practice in the industries in which the Company and its Subsidiaries operate and (iii) are in full force and effect. Neither the Company nor any of its Subsidiaries is in breach or default, and neither the Company nor any of its Subsidiaries have taken any action or failed to take any action which, with notice or the lapse of time, would constitute such a breach or default, or permit termination or modification, of any of the Policies. No notice of cancellation or termination has been received by the Company with respect to any of the Policies. The consummation of the Transactions will not, in and of itself, cause the revocation, cancellation or termination of any Policy.

Section 3.17 Brokers and Other Advisors. Except for Deutsche Bank Securities Inc., the fees and expenses of which will be paid by or on behalf of the Company, no broker, investment banker, financial advisor or other Person is entitled to any broker’s, finder’s, financial advisor’s or other similar fee or commission, or the reimbursement of expenses, in connection with the Transactions based upon arrangements made by or on behalf of the Company or any of its Subsidiaries. The Company has heretofore delivered to Parent a correct and complete copy of the Company’s engagement letter with Deutsche Bank Securities Inc., which letter describes all fees payable to Deutsche Bank Securities Inc. in connection with the Transactions, all agreements under which any such fees or any expenses are payable and all indemnification and other agreements related to the engagement of Deutsche Bank Securities Inc. (the “Engagement Letter”).

Section 3.18 Health Care Regulatory Compliance.

(a) Licensing Matters.

(i) The Company and each of its Subsidiaries owns, holds, possesses or lawfully uses all the permits, licenses, registrations, authorizations, bonds, accreditations, qualifications, provider numbers, rights, privileges, consents, certificates, orders, franchises, variances and approvals or other similar authorization issued by, or otherwise granted by, any Governmental Authority or accreditation body necessary or desirable for the ownership, use, or operation of its business including occupancy of any premises owned, leased or otherwise used by it (“Entity Permits”). Each manager, officer, member, employee and agent of the Company or of any of its Subsidiaries, as well as any director or shareholder of a Subsidiary (such Persons, collectively, “Company Representatives”) has all permits, licenses, registrations, authorizations, bonds, accreditations, qualifications, provider numbers, rights, privileges, consents, certificates, orders, franchises,
variances and approvals or other similar authorization issued by, or otherwise granted by, any Governmental Authority or accreditation body necessary or desirable for the performance of his or her duties for the Company and its Subsidiaries (“Individual Permits” and, together with Entity Permits, collectively, “Permits”). Section 3.18(a) of the Company Disclosure Schedules identifies all material Permits. The Company, its Subsidiaries, and the Company Representatives are in compliance with such Permits, all of which are in full force and effect, and have not received any notice (written or oral) to the contrary and there is no basis for believing that any Permit will not be renewable upon expiration without the need to comply with any special qualification procedures or to pay any amounts other than routine filing fees. None of such Permits will be adversely affected by consummation of the transaction contemplated hereby, none of such Permits will expire or terminate as a result of the consummation of the transaction contemplated hereby, and each such permit issued to or held by the Company or any of its Subsidiaries will continue in full force and effect following the Closing without requiring the consents or approval of any Person, assuming that there is no condition or circumstance applicable to Parent or its Subsidiaries immediately before the Closing that upon the Closing would cause any such Permit to expire or terminate. The Company, its Subsidiaries and the Company Representatives have not been a party to or subject to any proceeding seeking to revoke, suspend or otherwise limit any Permit of the Company, its Subsidiaries or any Company Representative. Neither the Company nor any of its Subsidiaries nor any Company Representative is in material breach or violation of, or default under, any such Permit. Neither the Company nor any of its Subsidiaries have received any notice from any Governmental Authority that any of its properties, facilities, equipment, operations or business procedures or practices fail to comply in any material respect with any applicable Law or Permit. Neither the Company nor any of its Subsidiaries are in breach or violation of any of the items listed in Section 3.18(a) of the Company Disclosure Schedules. There has been no decision by Company or its Subsidiaries not to renew any Permit relating to the business.

(ii) Neither the Company nor any of its Subsidiaries is involved in any litigation, proceeding, complaint, claim, charge, order or investigation pending, or to the Knowledge of Company threatened, by or with any Governmental Authority or accreditation body relating to any Permits, or alleged by such Governmental Authority or accreditation body to be required, for the operation of its business which, if determined or resolved adversely, would prevent it from doing business with any Governmental Authority, accreditation body, or any Person regulated by a Governmental Authority or accreditation body or have an adverse impact on the ability of the Company and its Subsidiaries to conduct business.

(b) Compliance with Health Care Laws. Except as set forth in Section 3.18(b) of the Company Disclosure Schedule, and without limiting the generality of any other representation or warranty made by the Company or any Subsidiary herein,
the Company and each of its Subsidiaries is conducting and has conducted its business and operations in compliance with, and neither the Company, any Subsidiary nor any of their respective officers, managers, directors, employees or shareholders has engaged in any activities that would constitute a violation of any applicable Healthcare Law. Except as set forth in Schedule 3.18(b) of the Company Disclosure Schedules:

(i) neither the Company nor any Subsidiary nor any Company Representative has received any written notice or communication from any Governmental Authority alleging noncompliance with any Healthcare Laws;

(ii) there is no civil, criminal or administrative action, suit, demand, claim, complaint, hearing, investigation, notice, demand letter, warning letter, proceeding or request for information related to noncompliance with, or otherwise involving, any Healthcare Laws pending against the Company or any Subsidiary or any Company Representative;

(iii) neither the Company or any Subsidiary has any material liability (whether actual or contingent) for failure to comply with any Healthcare Laws;

(iv) there has not been any violation of any Healthcare Laws by the Company or any Subsidiary in their respective submissions or reports to any governmental entity that could reasonably be expected to result in an investigation, corrective action or enforcement action;

(v) the Company and its Subsidiaries have maintained, in all material respects, all records required under any Healthcare Laws;

(vi) any remuneration exchanged between the Company or its Subsidiaries and their customers, suppliers, contractors, consultants or other entities with which they have a business relationship (collectively, “Trading Partners”) has at all times been commercially reasonable, negotiated at arms-length and represents the fair market value for rendered services.

(vii) the Company has properly documented, reported and disclosed to its customers and Government Authorities, as applicable, all manufacturer remuneration, including “discounts” or reductions in price (as defined in 42 U.S.C. § 1320a-7b(b)(3)(A)) and administrative fees, as required by any Healthcare Law and contractual requirements of manufacturers and health plans and is otherwise in full compliance with Healthcare Laws (including without limitation the provisions of ERISA) and contractual requirements of manufacturers and health plans regarding such discounts, reductions in price and administrative fees, and

(viii) the Company and its Subsidiaries are not relying on any exemption from or deferral of any Health Care Law that would not be available
after the Closing. To the Company’s knowledge, there are no pending changes in any Health Care Law that would prevent the Company from conducting the business after the Closing in substantially the same manner as currently conducted.

(c) Third-Party Payors. Except as disclosed in Section 3.18(c) of the Company Disclosure Schedules, Company and its Subsidiaries (a) do not participate under the programs provided by Titles XVIII and XIX of the Social Security Act (the “Medicare and Medicaid Programs”), the TRICARE Program (the Medicare and Medicaid Programs, the TRICARE Program, and such other similar federal, state or local reimbursement or governmental programs including “Federal health care programs” as defined in 42 U.S.C. § 1320a-7(b)(f)), (b) currently participate in the private, non-governmental programs (including any private insurance program) identified in Section 3.18(c) of the Company Disclosure Schedules under which Company and its Subsidiaries directly or indirectly is presently receiving payments (such private, non-governmental programs are referred to collectively as “Private Programs”), (c) are in good standing with the Private Programs, and (d) have no outstanding overpayments or refunds due to Government Programs or Private Programs in excess of $10,000. The Company and its Subsidiaries are operated in compliance with the conditions of participation of the Governmental Programs and Private Programs. The Company and its Subsidiaries have timely filed all claims and reports required to be filed prior to the date hereof with respect to the Governmental Programs and Private Programs, all fiscal intermediaries and/or carriers, and other insurance carriers, and all such claims and reports are complete and accurate in all material respects and have been prepared in material compliance with all applicable Law governing reimbursement and payment claims. Section 3.18(c) of the Company Disclosure Schedule identifies all additional document requests made by Governmental Programs or Private Programs to which Company or its Subsidiaries have not responded and all denials of claims currently being appealed by Company or its Subsidiaries. True and complete copies of all such claims, reports and other document requests filed or made since January 1, 2005 or for the year ended 2005 have been made available to Parent. The Company and its Subsidiaries have paid or caused to be paid all known and undisputed refunds, overpayments, discounts or adjustments that have become due pursuant to such claims and reports, have not claimed or received reimbursements from Governmental Programs or Private Programs in excess of the amounts permitted by applicable Law, and, to Company’s knowledge, have no liability under any Governmental Program or Private Program, other than any refund, overpayment, discount or adjustment that occurs in the ordinary course of business. Except as disclosed in Section 3.18 of the Company Disclosure Schedules, (i) there are no pending appeals, adjustments, challenges, litigation or notices of intent to audit and, to Company’s knowledge, no audits or inquiries with respect to such prior claims or reports, except for such appeals or individual claim denials that occur in the ordinary course of business and that, individually or in the aggregate, are not reasonably expected to have an adverse effect on the participation by the Company or any of its Subsidiaries in the Government Program or Private Program or involve an amount in excess of $10,000, and (ii) to the Company’s knowledge, the Company and its Subsidiaries have not been audited, surveyed or otherwise examined in connection with any Governmental Program.
or Private Program. Neither Company nor its Subsidiaries have received any notice indicating that its qualification as a participating provider in any Governmental Program or Private Program may be terminated or withdrawn, nor have any reason to believe that such qualification may be terminated or withdrawn. There has been no decision by Company or its Subsidiaries not to renew any third-party payor agreement relating to the business. All contracts with third-party payors were entered into by the Company in the ordinary course of business.

(d) **HIPAA Compliance.** The Company and its Subsidiaries are in all material respects in compliance, to the extent currently applicable, with the provisions of the Health Insurance Portability and Accountability Act of 1996 ("HIPAA") and all regulations promulgated pursuant to HIPAA, including the Transaction Code Set Standards, the Privacy Rules and the Security Rules set forth at 45 C.F.R. Parts 160 and 164.

(e) **Prescription Drug Purchases.** The Company’s purchase of prescription drugs and related items has at all times been conducted pursuant to the proper classification of the identity and status of the purchaser of such prescription drugs and/or related items and in accordance with all applicable Health Care Laws, Provider Agreements and Contracts.

(f) [Intentionally Omitted.]

(g) **Absence of Certain Business Practices.** Neither Company nor any of its Subsidiaries nor any Company Representative, nor any other Person or entity acting on behalf of Company or any of its Subsidiaries, acting alone or together, has in order to (A) obtain favorable treatment in securing business, (B) pay for favorable treatment for business secured, or (C) obtain special concessions or pay for special concessions already obtained for or in respect of Company or its Subsidiaries: (1) received, directly or indirectly, any rebates, payments, commissions, promotional allowances or any other economic benefits, regardless of their nature or type, from any customer, governmental employee or other person or entity with whom Company or its Subsidiaries has done business directly or indirectly, or (2) directly or indirectly, gave or agreed to give any contribution, gift, bribe, rebate, payoff, influence payment, kickback or similar benefit to any customer, governmental employee or other person or entity regardless of form, whether in money, property or services or (3) established or maintained any fund or asset that has not been recorded in the books and records of Company or its Subsidiaries.

(h) **Status of Persons.** Neither Company nor its Subsidiaries nor any Company Representative nor any other party to any Contract who furnishes services or supplies that may be reimbursed in whole or in part under any Governmental Program: (1) has been convicted of or charged with any violation of any Law related to any Governmental Program; (2) has been convicted of, charged with, or investigated for any violation of Law related to fraud, theft, embezzlement, breach of fiduciary responsibility, financial misconduct, obstruction of an investigation, or controlled substances; or (3) is excluded, suspended or debarred from participation, or is otherwise ineligible to
participate, in any Governmental Program or has committed any violation of Law that is reasonably expected to serve as the basis for any such exclusion, suspension, debarment or other ineligibility.

(i) Certain Financial Relationships. Section 3.18(i) of the Company Disclosure Schedule identifies all financial relationships (whether or not memorialized in writing), including any joint venture, partnership, co-ownership or other arrangement involving any ownership or investment interest, that the Company or any of its Subsidiaries have had, since the formation of the Company or such Subsidiary, with any individual known by the Company or any of its Subsidiaries to be a physician or an immediate family member of a physician, in connection with the business. For purposes of this section, the term “financial relationship” has the meaning set forth in 42 U.S.C. § 1395nn and the regulations promulgated thereunder.

SECTION 3.19 Accounts and Notes Receivable and Payable.

(a) All accounts and notes receivable of the Company and the Subsidiaries have arisen from bona fide transactions in the ordinary course of business consistent with past practice and are payable on ordinary trade terms. All accounts and notes receivable of the Company and the Subsidiaries reflected on the Balance Sheet are good and collectible at the aggregate recorded amounts thereof, net of any applicable reserve for returns or doubtful accounts reflected thereon, which reserves are adequate and were calculated in a manner consistent with past practice and in accordance with GAAP consistently applied. All accounts and notes receivable arising after the Balance Sheet Date and existing on the date hereof are good and collectible at the aggregate recorded amounts thereof, net of any applicable reserve for returns or doubtful accounts, which reserves are adequate and were calculated in a manner consistent with past practice and in accordance with GAAP consistently applied. None of the accounts or the notes receivable of the Company or any of the Subsidiaries (i) are subject to any setoffs or counterclaims or (ii) represent obligations for goods or services subject to any repurchase, return, refund or rebate arrangement.

(b) All accounts payable of the Company and the Subsidiaries reflected in the Balance Sheet or arising after the date thereof and existing on the date hereof are the result of bona fide transactions in the ordinary course of business consistent with past practice and have been paid or are not yet due and payable.

SECTION 3.20 Related Party Transactions. Except as set forth on Section 3.20 of the Company Disclosure Schedule, no employee, officer, manager, director, stockholder, partner or member of the Company or any of the Subsidiaries, or, to the Knowledge of the Company, any member of his or her immediate family or any of their respective Affiliates ("Related Persons") (i) owes any amount to the Company or any of the Subsidiaries nor does the Company or any of the Subsidiaries owe any amount to, or has the Company or any of the Subsidiaries made or committed to make any loan or guarantee of any credit or performance to or for the benefit of, any Related Person, (ii) is involved in any business arrangement or other relationship with the Company or any of
the Subsidiaries (whether written or oral), (iii) owns any property or right, tangible or intangible, that is used by the Company or any of the Subsidiaries, (iv) has any claim or cause of action against the Company or any of the Subsidiaries or (v) owns any direct or indirect interest of any kind in, or controls or is a director, officer, employee or partner of, or consultant to, or lender to or borrower from or has the right to participate in the profits of, any Person which is a competitor, supplier, customer, landlord, tenant, creditor or debtor of the Company or any Subsidiary.

SECTION 3.21  Banks; Power of Attorney. Section 3.21 of the Company Disclosure Schedule contains a complete and correct list of the names and locations of all banks in which Company or any Subsidiary has accounts or safe deposit boxes and the names of all persons authorized to draw thereon or to have access thereto. Except as set forth on Section 3.21 of the Company Disclosure Schedule, no person holds a power of attorney to act on behalf of the Company or any Subsidiary.

SECTION 3.22  Customers and Suppliers.

(a)  Section 3.22(a) of the Company Disclosure Schedule sets forth a list of all of the customers and all of the suppliers of the Company and the Subsidiaries, showing the approximate total sales by the Company and the Subsidiaries to each such customer and the approximate total purchases by the Company and the Subsidiaries from each such supplier, during the Company’s last fiscal year and during the current fiscal year through April 30, 2006.

(b)  Since the Balance Sheet Date, no customer or supplier listed on Section 3.22(a) of the Company Disclosure Schedule has terminated its relationship with the Company or any of the Subsidiaries or reduced or changed the pricing or other terms of its business with the Company or any of the Subsidiaries and, to the Knowledge of the Company or the Company Unitholders, no customer or supplier listed on Section 3.22(a) of the Company Disclosure Schedule has notified the Company or the Subsidiaries that it intends to terminate or reduce or change the pricing or other terms of its business with the Company or any of the Subsidiaries.

SECTION 3.23  Certain Payments. None of the Company, any Subsidiary or any Company Unitholder nor, to the Knowledge of the Company or the Company Unitholders, any director, officer, employee, or other Person associated with or acting on behalf of any of them, has directly or indirectly (a) made any contribution, gift, bribe, rebate, payoff, influence payment, kickback, or other payment to any Person, private or public, regardless of form, whether in money, property, or services (i) to obtain favorable treatment in securing business for the Company or any Subsidiary, (ii) to pay for favorable treatment for business secured by the Company or any Subsidiary, (iii) to obtain special concessions or for special concessions already obtained, for or in respect of the Company or any Subsidiary, or (iv) in violation of any Law, or (b) established or maintained any fund or asset with respect to the Company or any Subsidiary that has not be recorded in the books and records of the Company and the Subsidiaries.
SECTION 3.24  Full Disclosure. No representation or warranty of the Company contained in this Agreement (including the Company Disclosure Schedules) or any of the Company Documents and no written statement made by or on behalf of the Company to Parent (including any Representative thereof) pursuant to this Agreement or any of the Company Documents contains an untrue statement of a material fact or omits to state a material fact necessary to make the statements contained herein or therein not misleading.

SECTION 3.25  Employment Agreements With Key Employees. The Parent has, prior to the date hereof, entered into employment agreements (including agreements relating to holding of restricted shares of Parent, effective subject to and as of the Closing Date, with the individuals listed on Exhibit 3.25 and in the forms heretofore delivered to Parent and included as Section 3.25 of the Company Disclosure Schedules.

ARTICLE IV
Representations and Warranties of Parent and Merger Sub

Parent and Merger Sub jointly and severally make to the Company the representations and warranties contained in this Article IV:

SECTION 4.1  Organization, Standing and Corporate Power. Each of Parent, Acquiring Corp. and Merger Sub is a corporation duly organized, validly existing and in good standing under the Laws of the jurisdiction in which it is incorporated.

SECTION 4.2  Authority; Noncontravention.

(a) Each of Parent, Acquiring Corp. and Merger Sub has all necessary corporate power and authority to execute and deliver this Agreement and to perform their respective obligations hereunder and to consummate the Transactions. The execution, delivery and performance by Parent, Acquiring Corp. and Merger Sub of this Agreement, and the consummation by Parent, Acquiring Corp. and Merger Sub of the Transactions, have been duly authorized and approved by their respective Boards of Directors (and in the case of Merger Sub have been approved by Acquiring Corp. as the sole stockholder of Merger Sub) and no other corporate action on the part of Parent, Acquiring Corp. and Merger Sub is necessary to authorize the execution, delivery and performance by Parent, Acquiring Corp. and Merger Sub of this Agreement and the consummation by them of the Transactions. This Agreement has been duly executed and delivered by Parent, Acquiring Corp. and Merger Sub and, assuming due authorization, execution and delivery hereof by the Company, constitutes a legal, valid and binding obligation of each of Parent, Acquiring Corp. and Merger Sub, enforceable against each of them in accordance with its terms, subject to the Bankruptcy and Equity Exception.

(b) Neither the execution and delivery of this Agreement by Parent, Acquiring Corp. and Merger Sub, nor the consummation by Parent, Acquiring Corp. or Merger Sub of the Transactions, nor compliance by Parent, Acquiring Corp. or Merger Sub with any of the terms or provisions hereof, will (i) conflict with or violate any
provision of the certificate of incorporation or bylaws of Parent, Acquiring Corp. or Merger Sub or (ii) assuming that the authorizations, consents and approvals referred to in Section 4.3 are obtained and the filings referred to in Section 4.3 are made, (x) violate any Law, judgment, writ or injunction of any Governmental Authority or any arbitration award applicable to Parent or any of its Subsidiaries or any of their respective properties or assets, or (y) violate, conflict with, result in the loss of any benefit under, constitute a default (or an event which, with notice or lapse of time, or both, would constitute a default) under, result in the termination of or a right of termination or cancellation under, accelerate the performance required by, or result in the creation of any Lien upon any of the respective properties or assets of, Parent, Acquiring Corp. or Merger Sub or any of their respective Subsidiaries under, any of the terms, conditions or provisions of any Contract to which Parent, Acquiring Corp., Merger Sub or any of their respective Subsidiaries is a party, or by which they or any of their respective properties or assets may be bound or affected that, individually or in the aggregate, could reasonably be expected to adversely affect the ability of Parent, Acquiring Corp. or Merger Sub to perform, in a timely manner, its obligations under this Agreement or to consummate the Transactions.

SECTION 4.3 Governmental Approvals. Except for (i) the filing of the Certificate of Merger with the Secretary of State of the State of Delaware pursuant to the DGCL and (ii) filings required under, and compliance with other applicable requirements of, the HSR Act and (iii) the approvals or filings referred to in Schedule 4.4 delivered by Parent to the Company, no consents or approvals of, or filings, declarations or registrations with, any Governmental Authority are necessary for the execution and delivery of this Agreement by Parent, Acquiring Corp. and Merger Sub or the consummation by Parent, Acquiring Corp. and Merger Sub of the Transactions, other than such other consents, approvals, filings, declarations or registrations that, if not obtained, made or given, could not, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect with respect to Parent.

SECTION 4.4 Ownership and Operations of Acquiring Corp. and Merger Sub. Parent owns on the date hereof beneficially all of the outstanding capital stock of Acquiring Corp. and Merger Sub and, on the Closing Date, will own beneficially, directly or indirectly through one or more other wholly-owned direct or indirect subsidiaries, all of the outstanding capital stock of Acquiring Corp. and Merger Sub. Merger Sub was formed solely for the purpose of engaging in the Transactions, has engaged in no other business activities and has conducted its operations only as contemplated hereby.

SECTION 4.5 Brokers and Other Advisors. No broker, investment banker, financial advisor or other Person is entitled to any broker’s, finder’s, financial advisor’s or other similar fee or commission in connection with the Transactions based upon arrangements made by or on behalf of Parent or any of its Subsidiaries.

SECTION 4.6 Litigation. There is no suit, claim, action, proceeding or investigation pending or, to the Knowledge of Parent, threatened against Parent, Acquiring Corp. or Merger Sub and neither Parent, Acquiring Corp. nor Merger Sub is
subject to any outstanding order, writ, judgment, injunction or decree of any Governmental Authority that, in either case, would be reasonably likely, individually or in the aggregate, to (a) prevent or materially delay the consummation of the Merger or (b) otherwise prevent or materially delay performance by Parent, Acquiring Corp. or Merger Sub of any closing condition set forth in Section 6.2(d) or of their material obligations under this Agreement or (c) material to the business of Parent and its Subsidiaries taken as a whole.

ARTICLE V
Additional Covenants and Agreements

SECTION 5.1 Conduct of Business. Except as expressly required or permitted by this Agreement, as required by applicable Law or as permitted by the prior written consent of the Parent, during the period from the date of this Agreement until the earlier of the Effective Time or the termination of this Agreement pursuant to Article VII, the Company shall, and shall cause each of its Subsidiaries to, (i) conduct its business in the ordinary course consistent with past practice, (ii) comply in all material respects with all applicable Laws and the requirements of all Material Contracts, (iii) use commercially reasonable efforts to maintain and preserve intact its business organization and the goodwill of those having business relationships with it and retain the services of its present officers and key employees, in each case, to the end that its goodwill and ongoing business shall be unimpaired at the Effective Time, and (iv) keep in full force and effect all material insurance policies maintained by the Company and its Subsidiaries, other than changes to such policies made in the ordinary course of business. Without limiting the generality of the foregoing, except as expressly required or permitted by this Agreement, as required by applicable Law or as specified in Schedule 5.2 of the Company Disclosure Schedules or permitted by the prior written consent of the Parent, during the period from the date of this Agreement to the earlier of the Effective Time or the termination of this Agreement pursuant to Article VII, the Company shall not, and shall not permit any of its Subsidiaries to:

(a) (i) issue, sell, grant, dispose of, pledge or otherwise encumber any Company Units, other member interests, shares of capital stock, securities or equity interests in or of, or any securities, rights or options convertible into, or exchangeable or exercisable for, or evidencing the right to subscribe for, or any calls, commitments or any other agreements of any character to purchase or acquire, any Company Units or any member interests, shares of its capital stock, securities or equity interests in or of the Company or any Subsidiary, provided, however, that member interests, shares, securities or equity interests in or of the Company’s Subsidiaries may be issued to the Company or a direct or indirect wholly owned Subsidiary of the Company, (ii) redeem, purchase or otherwise acquire any of the outstanding Company Units or any member interests, shares, securities or equity interests in or of, or any options to acquire, any Company Units or any member interests, shares, securities or equity interests in or of, the Company or any Subsidiary of the Company; (iii) except as provided by the last sentence of this Section 5.1, declare, set aside for payment or pay any dividend on, or make any other distribution in respect of, the Company Units or any member interests, shares, securities or equity
(a) not make any distribution or payment, or create or incur any liability to make any distribution or payment, to the holders of interests in or of any Subsidiary, or otherwise make any payments to the holders thereof in their capacity as such (other than dividends by a direct or indirect wholly owned Subsidiary of the Company to its parent); (iv) split, combine, subdivide or reclassify any of the Company Units; or (v) amend (including by reducing the exercise price or extending the duration), or waive any of its rights under, any agreement evidencing any outstanding option or other right to acquire Company Units or any similar or related contract;

(b) incur or assume any indebtedness for borrowed money or guarantee any indebtedness (or enter into a “keep well” or similar agreement) or issue or sell any debt securities or options, warrants, calls or other rights to acquire any debt securities of the Company or any of its Subsidiaries;

(c) sell, transfer, lease, mortgage, encumber or otherwise dispose of or subject to any Lien (including pursuant to a sale-leaseback transaction or an asset securitization transaction), other than a Permitted Lien, any of its properties or assets (including securities of Subsidiaries) to any Person, except (i) pursuant to Contracts in force on the date of this Agreement and listed on Section 5.1(c) of the Company Disclosure Schedule, correct and complete copies of which have been made available to Parent, or (ii) dispositions of obsolete or worthless assets;

(d) make any capital expenditures, except in the ordinary course of business consistent with past practice and in an amount not in excess of $100,000 in the aggregate for the Company and its Subsidiaries taken as a whole during any three consecutive month period;

(e) directly or indirectly acquire (i) by merging or consolidating with, or by purchasing all of or a substantial equity interest in, or by any other manner, any Person or division, business or equity interest of any Person or (ii) except as permitted under Section 5.2(d), otherwise acquire any assets except in the ordinary course of business consistent with past practice, provided, further, that no such acquisition in the ordinary course of business of any assets that, individually, have a purchase price in excess of $100,000 or any group of related assets that, in the aggregate, have a purchase price in excess of $250,000 shall be made without reasonable prior notice to Parent and shall not be made over the Parent’s objection (which shall not be unreasonably interposed);

(f) make any investment (by contribution to capital, property transfers, purchase of securities or otherwise) in, or loan or advance (other than travel and similar advances to its employees in the ordinary course of business consistent with past practice) to, any Person other than a direct or indirect wholly owned Subsidiary of the Company in the ordinary course of business;

(g) (1) enter into, terminate or amend any Material Contract, or make any proposal to enter into, terminate, or amend any customer or client Contract, or, other than in the ordinary course of business consistent with past practice, any other Contract
that is material to the Company and its Subsidiaries taken as a whole, (2) enter into or extend the term or scope of any Contract that purports to restrict the Company, or any existing or future Subsidiary or Affiliate of the Company, from engaging in any line of business or in any geographic area, (3) amend or modify the Engagement Letter, (4) enter into any Contract that would be breached by, or require the consent of any third party in order to continue in full force following consummation of the Transactions, or (5) release any Person from, or modify or waive any provision of, any confidentiality, standstill or similar agreement or fail to take all action necessary to enforce each such confidentiality, standstill and similar agreement (in each case, other than any such agreement with Parent);

(h) increase in any manner the compensation of any of its directors, officers, managers or employees or enter into, establish, amend or terminate any employment, consulting, retention, change in control, collective bargaining, bonus or other incentive compensation, profit sharing, health or other welfare, option or other equity (or equity-based), pension, retirement, vacation, severance, deferred compensation or other compensation or benefit plan, policy, program, agreement, trust, fund or arrangement with, for or in respect of, any unitholder, director, officer, other employee, consultant or Affiliate, other than as required pursuant to applicable Law or the terms of an agreement, plan or program identified in Section 5.1(h) of the Company Disclosure Schedule (correct and complete copies of which have been made available to Parent);

(i) make or change any election concerning Taxes or Tax Returns, file any amended Tax Return, enter into any closing agreement with respect to Taxes, settle any Tax claim or assessment or surrender any right to claim a refund of Taxes or obtain any Tax ruling;

(j) make any changes in financial or tax accounting methods, principles or practices (or change an annual accounting period), except insofar as may be required by a change in GAAP or applicable Law;

(k) amend the Company Charter Documents or the Subsidiary Documents;

(l) adopt a plan or agreement of complete or partial liquidation, dissolution, restructuring, recapitalization, merger, consolidation or other reorganization (other than transactions exclusively between wholly owned Subsidiaries of the Company);

(m) except as provided by the last sentence of this Section 5.1, pay, discharge, settle or satisfy any material claims, liabilities or obligations (absolute, accrued, asserted or unasserted, contingent or otherwise), other than the payment, discharge, settlement or satisfaction in accordance with their terms of liabilities, claims or obligations reflected or reserved against in the most recent consolidated financial statements (or the notes thereto) of the Company or incurred since the date of such financial statements in the ordinary course of business consistent with past practice;
(n) issue any broadly distributed communication of a general nature to employees (including general communications relating to benefits and compensation) or customers or clients without the prior approval of Parent, except for communications in the ordinary course of business that do not relate to the Transactions or provide to any Person any Information regarding the Company (or its predecessor) that might be considered material non-public information (within the meaning of Regulation FD under the Exchange Act) if the Company’s securities were registered under Section 12(b) of the Exchange Act;

(o) settle or compromise any litigation, proceeding or investigation material to the Company and its Subsidiaries taken as a whole (this covenant being in addition to the Company’s agreement set forth in Section 5.9); or

(p) acquire any material properties or assets or sell, assign, license (other than non-exclusive licenses received from or granted to customers in the ordinary course of business consistent with past practice), transfer, convey, lease or otherwise dispose of any of the material properties or assets of the Company and its Subsidiaries;

(q) enter into, modify or terminate any labor or collective bargaining agreement of the Company or any of its Subsidiaries or, through negotiation or otherwise, make any commitment or incur any liability to any labor organization with respect to the Company or any of its Subsidiaries;

(r) enter into any Contract, understanding or commitment that restrains, restricts, limits or impedes the ability of the Company or any Subsidiary to compete with or conduct any business or line of business in any geographic area or enter into, or modify, amend or terminate, any Contract which would (1) cause the Company or any Subsidiary to incur a liability in excess of $100,000 or receive revenues in excess of $250,000, (2) have a term of more than one year (unless the Company or the Subsidiary may cancel such Contract in its discretion without incurring a liability in excess of such amount) or (3) could reasonably be expected to have a Material Adverse Effect on the Company (provided, however, that in no event will the Company be considered in breach of this clause (3) in connection with entering into a Contract after the date hereof as to which it has received the written consent of Parent); or

(s) agree, in writing or otherwise, to take any of the foregoing actions, or take any action or agree, in writing or otherwise, to take any action which would (1) cause any of the representations or warranties of the Company set forth in this Agreement to be untrue in any material respect or (2) in any material respect impede or delay the ability of the parties to satisfy any of the conditions to the Merger set forth in this Agreement.

Notwithstanding the foregoing provisions of this Section 5.1, the Company shall, immediately before the Closing, repay any indebtedness for borrowed money of the Company, other than any indebtedness for borrowed money owed to any Company Unitholder (or, earlier before the Closing do so in whole or in part consistent with the
operation of the business in the ordinary course). In addition, the Company shall make arrangements with the Company Unitholders so that, at the Closing, all expenses of the Company relating to the Transactions, including any investment banking or broker fees and expenses and any legal expenses and filing fees, and audit fees payable to Mayer Hoffman McCann, P.C., that have not already been paid shall have been paid in full before or at the Closing so that the Company upon the Closing shall have no liability therefor. Also notwithstanding the foregoing provisions of this Section 5.1, the Company shall, immediately before the Closing, cause the existing lien against the Company’s assets in favor of its supplier Cardinal Health, Inc. and any other similar lien on the Company’s assets (other than a Permitted Lien), to be removed (including, if necessary, by Company Unitholders providing cash collateral to secure such obligations in lieu of such obligations being secured by other assets of the Company) and deliver evidence reasonably satisfactory to the Company of the removal of such lien.

SECTION 5.2 No Solicitation by the Company; Etc.

(a) The Company shall, and shall cause its Subsidiaries and the Company’s and its Subsidiaries’ respective directors, officers, managers, employees, investment bankers, financial advisors, attorneys, accountants, agents and other representatives (collectively, “Representatives”) to, immediately cease and cause to be terminated any discussions or negotiations with any Person conducted heretofore with respect to a Takeover Proposal. The Company shall not, and shall cause its Subsidiaries and Representatives not to, directly or indirectly (1) solicit, initiate, cause, facilitate or knowingly encourage (including by way of furnishing information) any inquiries or proposals that constitute, or would reasonably be expected to lead to, a Takeover Proposal, and use its commercially reasonable efforts to obtain the return from all such Persons, or to cause the destruction of, all copies of confidential information previously provided to such parties by the Company, its Subsidiaries or Representatives, (2) participate in any discussions or negotiations with any third party regarding any Takeover Proposal or (3) enter into any agreement related to any Takeover Proposal.

(b) In addition to the other obligations of the Company provided by this Agreement, the Company shall promptly advise Parent, orally and in writing, and in no event later than 24 hours after receipt, if any proposal, offer, inquiry or other contact is received by, any information is requested from, or any discussions or negotiations (or continuation of discussions or negotiations) are sought to be initiated with, the Company in respect of any Takeover Proposal, and shall, in any such notice to Parent, indicate the identity of the Person making such proposal, offer, inquiry or other contact and the terms and conditions of any proposals or offers or the nature of any inquiries or contacts (and shall include with such notice copies of any written materials received from or on behalf of such Person relating to such proposal, offer, inquiry or request), and thereafter shall promptly keep Parent fully informed of all material developments affecting the status and terms of any such proposals, offers, inquiries or requests (and the Company shall provide Parent with copies of any additional written materials received that relate to such proposals, offers, inquiries or requests) and of the status of any such discussions or negotiations.
For purposes of this Agreement, “Takeover Proposal” means any inquiry, proposal or offer from any Person relating to any (A) direct or indirect acquisition (whether in a single transaction or a series of related transactions) of assets of the Company and its Subsidiaries (including securities of Subsidiaries), (B) direct or indirect acquisition (whether in a single transaction or a series of related transactions) of Company Units or member interests, shares of capital stock, securities or equity interests in or of the Company or any Subsidiary, or (C) merger, consolidation, share exchange, business combination, recapitalization, liquidation, dissolution or similar transaction involving the Company or any of its Subsidiaries; in each case, other than the Transactions.

SECTION 5.3 Best Efforts.

(a) Lender Consent. Parent shall use its best efforts to obtain, as soon as practicable after the date hereof, the consent required under the Credit Agreement to permit it and its Subsidiaries to consummate the Transactions. Parent shall keep Company reasonably informed of the progress of its efforts to obtain such consent. If Parent has not received the consent so required under the Credit Agreement within thirty (30) days of the date hereof, Parent will use its best efforts to refinance the Credit Agreement on terms permitting it and its Subsidiaries to consummate the Transactions.

(b) Subject to the terms and conditions of this Agreement (including Section 5.4(d)), each of the parties hereto shall cooperate with the other parties and use (and shall cause their respective Subsidiaries to use) their respective commercially reasonable efforts to (i) take, or cause to be taken, all actions, and do, or cause to be done, all things, necessary, proper or advisable to cause the conditions to Closing to be satisfied as promptly as practicable and to consummate and make effective, in the most expeditious manner practicable, the Transactions, including preparing and filing promptly and fully all documentation to effect all necessary filings, notices, petitions, statements, registrations, submissions of information, applications and other documents (including any required or recommended filings under applicable Antitrust Laws), and (ii) obtain all approvals, consents, registrations, permits, authorizations and other confirmations from any Governmental Authority or third party necessary, proper or advisable to consummate the Transactions. For purposes hereof, “Antitrust Laws” means the Sherman Act, as amended, the Clayton Act, as amended, the HSR Act, the Federal Trade Commission Act, as amended, and all other applicable Laws issued by a Governmental Authority that are designed or intended to prohibit, restrict or regulate actions having the purpose or effect of monopolization or restraint of trade or lessening of competition through merger or acquisition.

(c) In furtherance and not in limitation of the foregoing, (i) each party hereto agrees to make an appropriate filing of a Notification and Report Form pursuant to the HSR Act with respect to the Transactions as promptly as practicable and in any event within three (3) business days of the date hereof and to supply as promptly as practicable any additional information and documentary material that may be requested pursuant to the HSR Act and use its reasonable best efforts to take, or cause to be taken, all other
actions consistent with this Section 5.4 necessary to cause the expiration or termination of the applicable waiting periods under the HSR Act as soon as practicable. Parent covenants and agrees that it shall be solely responsible for the filings or related fees incurred by Parent and the Company in connection with the aforementioned filings under the HSR Act.

(d) Each of the parties hereto shall use its reasonable best efforts to (i) cooperate in all respects with each other in connection with any filing or submission with a Governmental Authority in connection with the Transactions and in connection with any investigation or other inquiry by or before a Governmental Authority relating to the Transactions, including any proceeding initiated by a private party, and (ii) keep the other party informed in all material respects and on a reasonably timely basis of any material communication received by such party from, or given by such party to, the Federal Trade Commission, the Antitrust Division of the Department of Justice, or any other Governmental Authority and of any material communication received or given in connection with any proceeding by a private party, in each case regarding any of the Transactions. Subject to applicable Laws relating to the exchange of information, each of the parties hereto shall have the right to review in advance, and to the extent practicable each will consult the other on, all the information relating to the other party and their respective Subsidiaries, as the case may be, that appears in any filing made with, or written materials submitted to, any third party and/or any Governmental Authority in connection with the Transactions.

(e) In furtherance and not in limitation of the covenants of the parties contained in this Section 5.4, each of the parties hereto shall use its reasonable best efforts to resolve such objections, if any, as may be asserted by a Governmental Authority or other Person with respect to the Transactions. Notwithstanding the foregoing or any other provision of this Agreement, the Company shall not, without Parent’s prior written consent, commit to any divestiture transaction or agree to any restriction on its business, and nothing in this Section 5.4 shall (i) limit any applicable rights a party may have to terminate this Agreement pursuant to Section 7.1 so long as such party has up to then complied in all material respects with its obligations under this Section 5.4 or (ii) require Parent to offer, accept or agree to (A) dispose or hold separate any part of its or the Company’s businesses, operations, assets or product lines (or a combination of Parent’s and the Company’s respective businesses, operations, assets or product lines), (B) not compete in any geographic area or line of business, and/or (C) restrict the manner in which, or whether, Parent, the Company, the Surviving company or any of their Affiliates may carry on business in any part of the world.

SECTION 5.4 Public Announcements. The initial press release with respect to the execution of this Agreement shall be a joint press release to be reasonably agreed upon by Parent and the Company. Thereafter, neither the Company nor Parent shall issue or cause the publication of any press release or other public announcement (to the extent not previously issued or made in accordance with this Agreement) with respect to the Merger, this Agreement or the other Transactions without the prior consent of the other party (which consent shall not be unreasonably withheld or delayed), except as may
be required by Law or in the case of the Parent by its listing agreement with Nasdaq as determined in its good faith judgment (in which case such party shall not issue or cause the publication of such press release or other public announcement without prior consultation insofar as practicable with the Company).

SECTION 5.5 Access to Information; Confidentiality. Subject to applicable Laws relating to the exchange of information, the Company agrees that, prior to the Effective Time or the termination of this Agreement in accordance with Article VII, Parent shall be entitled, through its officers, employees and representatives (including its legal advisors and accountants), to make such investigation of the properties, businesses and operations of the Company and its Subsidiaries and such examination of the books, records and financial condition of the Company as it reasonably requests and to make extracts and copies of such books and records. No investigation by Parent prior to or after the date of this Agreement shall diminish or obviate any of the representations, warranties, covenants or agreements of the Company contained in this Agreement or the Company Documents. Any such investigation by Parent shall not unreasonably interfere with any of the businesses or operations of the Company and its Subsidiaries. Neither Parent nor any of its officers, employees or representatives shall, prior to the Closing Date, have any contact whatsoever with any customer, lender, lessor, vendor, supplier, employee or consultant of the Company and its Subsidiaries, except in consultation with the Company and then only with the express prior approval of the Company, which approval shall not be unreasonably withheld. All requests by Parent for access or information shall be submitted or directed exclusively to an individual or individuals to be designated by the Company. In order that Parent may have full opportunity to make such physical, business, accounting and legal review, examination or investigation as it may reasonably request of the affairs of the Company and its Subsidiaries, the Company shall use commercially reasonable efforts to cause the officers, employees, consultants, agents, accountants, attorneys and other representatives of the Company and its Subsidiaries to cooperate fully with such representatives in connection with such review and examination. Except for disclosures permitted by the terms of the Confidentiality Agreement, dated as of March 15, 2006, between Parent and the Company (as it may be amended from time to time, the "Confidentiality Agreement"), Parent and its Representatives shall hold information received from the Company pursuant to this Section 5.6 in confidence in accordance with the terms of the Confidentiality Agreement.

SECTION 5.6 Notification of Certain Matters. The Company shall give prompt written notice to Parent, and Parent shall give prompt written notice to the Company, of (i) any notice or other communication received by such party from any Governmental Authority in connection with the Transactions or from any Person alleging that the consent of such Person is or may be required in connection with the Transactions, (ii) any actions, suits, claims, investigations or proceedings commenced or, to such party’s knowledge, threatened against or otherwise involving such party or any of its Subsidiaries or Affiliates which relate to the Transactions, (iii) the discovery of any fact or circumstance that, or the occurrence or
non-occurrence of any event the occurrence or non-occurrence of which, would cause any representation or warranty made by such party contained in this Agreement (A) that is qualified as to materiality to be untrue or (B) that is not so qualified to be untrue in any material respect or, in the case of the Company, would cause any of the information provided in the Company Disclosure Schedules to not be true and correct as of the time such information was provided in light of such discovery or occurrence or non-occurrence, and (iv) any material failure of such party to comply with or satisfy any covenant or agreement to be complied with or satisfied by it hereunder; provided, however, that the delivery of any notice pursuant to this Section 5.6 shall not (x) cure any breach of any representation of warranty of the party giving such notice or any non-compliance by the party giving such notice with any covenant, agreement or other provision contained in this Agreement or (y) limit the remedies available to the party receiving such notice in respect of such breach or non-compliance.

SECTION 5.7 Intentionally Omitted.

SECTION 5.8 Fees and Expenses. Except as may otherwise be provided herein, all fees and expenses incurred in connection with this Agreement, the Merger and the Transactions shall be paid by the party incurring such fees or expenses, whether or not the Merger is consummated.

SECTION 5.9 Change In Control Customer Contracts. The Company shall, prior to the Closing Date, (i) notify each third party to the Change In Control Customer Contracts listed on Section 3.13 of the Company Disclosure Schedule of the Transactions and (ii) request and receive a waiver, if required, of any termination rights arising as a result of the Transactions from each such party.

SECTION 5.10 Tax Matters. (a) Parent and the Unitholder Representative agree to allocate the Merger Consideration and liabilities of the Company existing immediately prior to the Closing to the assets of the Company based on the fair market value of such assets within ninety (90) days after the Closing. Such allocation shall be prepared by Parent and delivered to the Unitholder Representative as of the Closing (the “Allocation Schedule”). Within thirty (30) days after the Unitholder Representative’s receipt of the Allocation Schedule, initial or revised, as the case may be, the Unitholder Representative shall indicate its concurrence therewith, or propose to Parent any changes to such Allocation Schedule. The Unitholder Representative’s failure to notify Parent of any objection to such Allocation Schedule within thirty (30) days after receipt thereof shall constitute the Unitholder Representative’s concurrence therewith. The Unitholder Representative and Parent will negotiate in good faith to resolve any disputes regarding the Allocation Schedule. If the Unitholder Representative and Parent are unable to resolve any disputes regarding the Allocation Schedule within thirty (30) days of Parent’s receipt of such changes, then such dispute will be submitted to the Independent Accounting Firm for resolution as soon as practicable. The Independent Accounting Firm shall act as an expert and not as an arbitrator to determine, based solely on the written submissions of the
parties and not by independent investigation, only the specific items under dispute by the parties. Each of the Parent, Unitholder Representative and the Company (as applicable) shall complete and timely file all forms and statements (and any exhibits thereto), including Tax Returns, required by applicable Tax laws, in accordance with the Allocation Schedule, as revised from time to time as provided herein, in accordance with applicable Tax laws, and none of them shall take a position on any Tax Return or other form or statement contrary with such allocation.

(b) The Company shall prepare (or cause to be prepared) and file (or cause to be filed) when due (taking into account all extensions properly obtained) all Tax Returns required to be filed by or with respect to the Company or any of its Subsidiaries on or prior to the Closing Date. All such Tax Returns shall be prepared in a manner consistent with past practice; provided that there is a reasonable basis for the positions claimed on such Tax Returns. The Company shall deliver to Parent copies of each such Tax Return at least twenty (20) days prior to the due date for filing such Tax Return, and shall permit Parent to review and approve such Tax Return prior to filing (which approval shall not be unreasonably withheld or delayed). If the parties have not resolved any dispute relating to any such Tax Return prior to the due date for filing such Tax Return, then the Company shall file such Tax Return as prepared, but such filing shall not prejudice the rights of any party to pursue such dispute.

(c) Parent and Company recognize that, for federal income tax purposes and for state income tax purposes, the Company will file a final partnership tax return for the period ending at the Closing Date, and there will be no Straddle Period. The Unitholder Representative will cause to be prepared and filed the final partnership income tax returns, subject to Parent’s review and approval, which shall not be unreasonably withheld.

(d) Following the Closing, Parent shall prepare (or cause to be prepared) and file (or cause to be filed) when due (taking into account all extensions properly obtained) all Tax Returns, other than the Company final partnership return described in Section 5.10(c), required to be filed by or with respect to the Company or any of its Subsidiaries after the Closing Date in respect of any Pre-Closing Tax Period or Straddle Period. A copy of any such Tax Return with respect to which Tax is owing and for which the Company Unitholders are liable pursuant hereto shall be delivered to the Unitholder Representative, along with a statement (a “Tax Statement”) showing the Unitholder Representative’s share of any Taxes owed that are reflected on such Tax Return (which shall be computed in accordance with Section 8.2(e)), at least twenty (20) days prior to the due date for filing such Tax Return, and shall permit the Unitholder Representative to review and approve such Tax Return and Tax Statement prior to filing (which approval shall not be unreasonably withheld or delayed). If the parties have not resolved any dispute relating to any such Tax Return prior to the due date for filing such Tax Return, then Parent shall file such Tax Return as prepared, but such filing shall not prejudice the rights of any party to pursue such dispute.
(e) Not later than two (2) days prior to the due date for the payment of Taxes on any Tax Returns relating to Pre-Closing Periods or Straddle Periods which Parent has the responsibility to file (or cause to be filed) pursuant to Section 5.10(b), the Parent shall reduce the amount of the Deferred Payment by the amount shown on the corresponding Tax Statement; provided, however, that, in the event that the Unitholder Representative disputes the amount shown on the Tax Statement, the dispute resolution provisions of Section 8.3(c) shall apply and the Deferred Payment shall not be considered reduced by the contested amount of the Tax Statement until the dispute is resolved. No payment pursuant to this Section 5.10(e) shall excuse the Unitholder Representative from its indemnification obligations pursuant to Section 8.2 if the amount of Taxes as ultimately determined (on audit or otherwise) for the periods covered by such Tax Returns exceeds the funds distributed or available to be distributed from the Withhold under this Section 5.10(e).

(f) In order to apportion appropriately any Taxes relating to Straddle Periods, the parties hereto will, to the extent permitted by applicable Law, elect with the relevant taxing authority to treat for all purposes the Closing Date as the last day of a taxable period of the Company (a “Short Period”). In any case where applicable Law does not permit the Company to treat the Closing Date as the last day of a Short Period, then for purposes of this Agreement, the portion of each Tax that is attributable to the operations of the Company for the period which would have qualified as a Short Period if such election had been permitted by applicable Law (an “Interim Period”) shall be (1) in the case of a Tax that is not based on net income or receipts, the total amount of such Tax for the period in question multiplied by a fraction, the numerator of which is the number of days in the Interim Period, and the denominator of which is the total number of days in such Straddle Period, and (ii) in the case of a Tax that is based on net income or receipts, the Tax that would be due with respect to the Interim Period if such Interim Period were a Short Period determined based upon an interim closing of the books.

(g) Notwithstanding anything to the contrary contained in this Agreement, Parent shall have the sole right to control, through counsel of its own choosing, the defense or settlement of any claim or proceeding relating to a Tax Loss; provided that, with respect to any Tax Loss for which the Unitholder Representative otherwise shall be liable under the indemnification provisions hereunder, Parent (i) shall keep the Unitholder Representative apprised of all developments relating to such claim or proceeding, (ii) shall provide the Unitholder Representative with copies of all correspondence from any taxing authority relating to any such claim or proceeding, (iii) shall provide the Unitholder Representative in advance with any proposed submission relating to such claim or proceeding, (iv) shall consult with the Unitholder Representative in good faith concerning any such submission and the conduct of the proceeding, and (v) shall not finally settle any such claim or proceeding without the prior written consent of Unitholder Representative (which consent shall not be unreasonably withheld or delayed).

(h) Each party hereto agree to co-operate fully, as and to the extent reasonably requested by the other party, in connection with the filing of any Tax Returns,
any audit, litigation or other proceeding with respect to Taxes. The parties further agree, upon request, to use their commercially reasonable efforts to obtain any certificate or other document from any taxing authority or any other Person as may be necessary to mitigate, reduce or eliminate any Tax that could be imposed with respect to the transactions contemplated in this Agreement.

(i) All transfer, documentary, sales, use, registration, stamp and similar Taxes and fees (including penalties and interest) incurred in connection with the transactions contemplated by this Agreement shall be borne equally by the Company Unitholders and Parent.

SECTION 5.11 Employment Agreements. The Company shall not, without the prior written consent of Parent, take any action to amend or terminate the employment agreements identified on Exhibit 3.25.

ARTICLE VI
Conditions Precedent

SECTION 6.1 Conditions to Each Party’s Obligation to Effect the Merger. The respective obligations of each party hereto to effect the Merger shall be subject to the satisfaction (or waiver, if permissible under applicable Law) on or prior to the Closing Date of the following conditions:

(a) Antitrust Clearance. The waiting period (and any extension thereof) applicable to the Merger under the HSR Act shall have been terminated or shall have expired; and

(b) No Injunctions or Restraints. No Law, injunction, judgment or ruling enacted, promulgated, issued, entered, amended or enforced by any Governmental Authority, and no arbitration award, enjoining, restraining, preventing or prohibiting consummation of the Merger or making the consummation of the Merger illegal (collectively, “Restraints”) shall be in effect.

SECTION 6.2 Conditions to Obligations of Parent, Acquiring Corp. and Merger Sub. The obligations of Parent, Acquiring Corp. and Merger Sub to effect the Merger are further subject to the satisfaction (or waiver, if permissible under applicable Law) on or prior to the Closing Date of the following conditions:

(a) Representations and Warranties. The representations and warranties of the Company contained in this Agreement including, without limitation, in the Company Disclosure Schedules (and without giving any effect to any notice given by the Company pursuant to Section 5.6), are true and correct in all material respects, in each case as of the date of this Agreement and as of the Closing Date as though made on and as of the Closing Date, except to the extent such representations and warranties expressly state that they are as of an earlier date in which case as though made on the Closing Date as of such earlier date; and Parent shall have received a certificate signed on
behalf of the Company by the chief executive officer and the chief financial officer of the Company to such effect. In addition, the chief executive officer and the chief financial officer of the Company shall have provided to the Parent as of the Closing Date the certifications with regard to the Company’s control over financial reporting and other matters provided by Exhibit 6.2(a).

(b) **Performance of Obligations of the Company.** The Company shall have performed in all material respects all obligations required to be performed by it under this Agreement at or prior to the Closing Date, and Parent shall have received a certificate signed on behalf of the Company by the chief executive officer and the chief financial officer of the Company to such effect.

(c) **No Company Material Adverse Effect.** No event, change in circumstances or state of facts shall have occurred or been discovered since the date of this Agreement that has had, or could reasonably be expected to have, a Material Adverse Effect on the Company.

(d) **Resolutions, Etc.** The Manager of the Company shall deliver a certificate to Parent certifying as to actions taken by the Manager and members of the Company approving the Transactions or otherwise relating to the Transactions, as Parent shall reasonably request.

(e) **No Litigation, Etc.** There shall not be any action, investigation, proceeding or litigation instituted, commenced, pending or threatened by or before any Governmental Authority or arbitrator that would, or that seeks to or is reasonably likely to, (i) restrain, enjoin, prevent, prohibit or make illegal the acquisition of some or all of the Company Units by Parent or Merger Sub or the consummation of the Merger or the other Transactions, (ii) impose limitations on the ability of Parent or its Affiliates effectively to exercise full rights of ownership of all shares of the Surviving Company including the right to vote all such shares on all matters properly presented to unitholders, (iii) restrain, enjoin, prevent, prohibit or make illegal, or impose limitations on, Parent’s or any of its Affiliates’ ownership or operation of all or any material portion of the businesses and assets of the Company and its Subsidiaries, taken together as a whole), (iv) as a result of the Transactions, restrain, enjoin, prevent, prohibit or make illegal, or impose limitations on, any portion of the businesses or assets of Parent or any of its Subsidiaries or would, or is reasonably likely to, result in a Governmental Investigation of being commenced or continued after the Effective Time or in Governmental Damages being imposed on the Surviving company or Parent or any of their respective Affiliates, (v) as a result of the Transactions, compel Parent or any of its Affiliates to dispose of any shares of the Surviving company or to dispose of or hold separate any material portion of the businesses or assets of the Company and its Subsidiaries (taken together as a whole) or any Portion of the business or assets of Parent and its Subsidiaries, or (vi) impose damages (other than Governmental Damages referred to in the foregoing clause (iv) of this sentence) on Parent, the Company or any of their respective Subsidiaries as a result of the Transactions in amounts that are material in relation to the Company or the Transactions. As used herein, (i) "Governmental Damages" shall mean (A) any penalties...
or fines paid or payable to a Governmental Authority or (B) any restitution paid or payable to a third party, in either case as a result of the (x) conviction (including as a result of the entry of a guilty plea, a consent judgment or a plea of nolo contendere) of the Company or any of its Subsidiaries of a crime or (y) a settlement with a Governmental Authority for the purpose of closing a Governmental Investigation; provided, however, that any de minimis penalties, fines or payments shall not be deemed to be Governmental Damages; and (ii) "Governmental Investigation" shall mean an investigation by a Governmental Authority for the purpose of imposing criminal sanctions.

(f) **Required Consents.** The Company shall have obtained all consents, waivers and approvals, and given all of the notices, referred to in Section 3.13(b) of the Company Disclosure Schedule, each such consent, waiver and approval is in form and substance reasonably satisfactory to Parent and does not require as a term thereof or condition thereto satisfaction of any adverse condition or requirement on the conduct of business by the Company, any of its Subsidiaries, Parent or any of its Subsidiaries.

(g) **Regulatory Consents.** The Company shall have obtained all required regulatory consents, waivers and approvals, and given all notices to Governmental Authorities, identified on Schedule 3.18(a) of the Company Disclosure Schedule.

(h) **Employment Agreements; Subscription Agreements.** All individuals identified on Exhibit 3.25 shall be able and willing, as of the Effective Time, to serve as employees of the Company under the employment agreements identified on Exhibit 3.25. All of the persons identified on Schedule 3.3(c) of the Company Disclosure Schedules shall be able and willing, as of the Effective Time, to perform their respective obligations under the Subscription Agreements.

(i) **FIRPTA Certificate.** Parent shall have received a statement issued by the Company as described in Treasury Regulation Section 1.1445-2(c)(3) and in a form reasonably satisfactory to Parent certifying that the Company Units are not U.S. real property interests as such term is defined in Code Section 897(c).

(j) **Good Standing Certificates.** The Company shall have delivered, or caused to be delivered, to Parent certificates of good standing as of a recent date with respect to each of the Company and Oncore issued by the Secretary of State of the State of Delaware and appropriate certificates attesting to its authorization to do business in each state in which the Company or Oncore is qualified to do business (except for such states the failure to qualify in which would not be reasonably expected to have a Material Adverse Effect on the Company).

(k) **Consent of Lender.** Parent shall have obtained the required consents under the Credit Agreement in order for it to consummate the Transactions without causing a default thereunder, or failing to obtain such consent, shall have
consummated a refinancing of the Credit Agreement in accordance with its obligations under Section 5.3 hereof.

(l) **Certification of Closing Conditions.** Parent shall have received a certificate signed by each of the chief executive officer and chief financial officer of the Company, each in form and substance reasonably satisfactory to Parent, dated the Closing Date, to the effect that, to his Knowledge, each of the conditions specified above in Sections 6.1(a) through (j) have been satisfied.

SECTION 6.3 **Conditions to Obligation of the Company.** The obligation of the Company to effect the Merger is further subject to the satisfaction (or waiver, if permissible under applicable Law) on or prior to the Closing Date of the following conditions:

(a) **Representations and Warranties.** The representations and warranties of Parent, Acquiring Corp. and Merger Sub contained in this Agreement that are qualified as to materiality or Parent Material Adverse Effect shall be true and correct, and the representations and warranties of Parent and Merger Sub contained in this Agreement that are not so qualified shall be true and correct in all material respects, in each case as of the date of this Agreement and as of the Closing Date as though made on the Closing Date, except to the extent such representations and warranties expressly relate to an earlier date, in which case as of such earlier date, and the Company shall have received a certificate signed on behalf of Parent by an executive officer of Parent to such effect.

(b) **Performance of Obligations of Parent, Acquiring Corp. and Merger Sub.** Parent, Acquiring Corp. and Merger Sub shall have performed in all material respects all obligations required to be performed by them under this Agreement at or prior to the Closing Date and the Company shall have received a certificate signed on behalf of Parent by an executive officer of Parent to such effect.

SECTION 6.4 **Frustration of Closing Conditions.** None of the Company, Acquiring Corp. Parent or Merger Sub may rely on the failure of any condition set forth in Section 6.1, 6.2 or 6.3, as the case may be, to be satisfied as grounds for its not consummating the Merger when otherwise required hereunder if such failure was caused by such party’s failure to use its commercially reasonable efforts to consummate the Merger and the other Transactions, as required by and subject to the provisions of Section 5.3.

ARTICLE VII
Termination

SECTION 7.1 **Termination.** This Agreement may be terminated and the Transactions abandoned at any time prior to the Effective Time:
(a) by the mutual written consent of the Company and Parent duly authorized by each of their respective Boards of Directors or equivalent body (or a duly authorized committee thereof); or

(b) by either of the Company or Parent:

if the Merger shall not have been consummated on or before September 30, 2006 or, if the consents referred to in Sections 6.2(f) or 6.2(k) have not been received consistent with the requirements of such sections by September 30, 2006 (the "Walk-Away Date"), then the right to terminate this Agreement under this Section 7.1(b)(i) shall not be available to a party if the failure of the Merger to have been consummated on or before the Walk-Away Date was primarily due to the failure of such party to perform any of its obligations under this Agreement; or

(i) if any Restraint having the effect set forth in Section 6.1(b) shall be in effect and shall have become final and nonappealable or if any Restraint resulting from any judicial or administrative injunction, judgment, order or any arbitration award is in effect and, although such injunction, judgment, order or award is subject to appeal or review and, as a result, to being reversed, over-ruled, dissolved or revoked, in the good faith judgment of the Company or the Parent, as the case may be, such reversal, over-ruling, dissolution or revocation cannot reasonably be expected to occur before the Walk-Away Date; provided, however, that the right to terminate this Agreement under this Section 7.1(b)(ii) shall not be available to a party if such Restraint was primarily due to the failure of such party to perform any of its obligations under this Agreement; or

(c) by Parent:

(i) if the Company shall have breached any of its representations or warranties (or if any of the representations or warranties of the Company set forth in this Agreement shall fail to be true and correct) or if the Company has breached or failed to perform or adhere to any of its covenants or agreements (including, without limitation, any failure to comply with Section 5.2(a)) set forth in this Agreement, which breach or failure (A) would, if it occurred or was continuing on the Closing Date, give rise to the failure of a condition set forth in Section 6.2(a) or (b) and (B) is not cured by the Company within ten calendar days following receipt of written notice from Parent of such breach or failure or is incapable of being cured before the Walk-Away Date; or

(ii) after the date of this Agreement there shall have occurred any events or changes in circumstances or states of fact that, individually or in the aggregate, have had or could reasonably be expected to have a Material Adverse Effect on the Company; or

SECTION 7.2 Means and Effect of Termination. In the event the Company or Parent wishes to terminate this Agreement as provided in
written notice thereof shall be given to the other parties, specifying the provision hereof pursuant to which such termination is made, and this Agreement shall forthwith become null and void (other than the provisions of the first sentence of Section 3.17, the first sentence of Section 4.5, Sections 5.4, 5.5 and 5.8, this Section 7.2 and, insofar as pertinent to the application of this Section 7.2, Article IX, all of which shall survive termination of this Agreement), and there shall be no other liability on the part of Parent, Merger Sub or the Company or their respective directors, officers, employees or Affiliates in connection therewith, provided that nothing herein shall relieve any party from liability for fraud or any willful breach of this Agreement.

ARTICLE VIII
Survival of Representations, Warranties and Covenants; Indemnification

SECTION 8.1 Survival of Representations, Warranties and Covenants

(a) Survival of Representations and Warranties. The representations and warranties of Parent contained in this Agreement shall survive the Closing for one year from the Closing Date. The representations and warranties of the Company contained in this Agreement shall survive the Closing until the third anniversary of the Closing Date (the “Expiration Date”), provided, however, that the representations and warranties of the Company set forth in Section 3.10 (taxes) and Section 3.18 (health regulatory compliance) shall survive the Closing indefinitely until ninety (90) days following the expiration of the applicable statute of limitations with respect to a claim by a third party that, if true, would constitute a breach of such representation and warranty. Any claim of breach of a representation or warranty contained herein not set forth in reasonable detail (based on the factual information then reasonably available to the claimant) by written notice to the party who is claimed to have breached such representation or warranty before the expiration of the period of survival of such representation or warranty provided hereby is hereby barred, may not be pursued and is hereby irrevocably waived as of the expiration of such survival period.

(b) Survival of Covenants. All covenants and agreements of the parties made in this Agreement which contemplate performance following the Closing shall survive the Closing in accordance with their terms. All covenants and agreements of the parties made in this Agreement that contemplate performance prior to the Closing shall not survive the Closing; provided, however, that (1) if any such covenant or agreement was breached by Parent on or prior to the Closing, the Company Unitholders shall nevertheless have in respect of such breach the rights and remedies provided by law if, but only if, written notice of such breach is given to Parent before the first anniversary of the Closing Date. and (2) if any such covenant or agreement was breached by the Company on or prior to the Closing, Parent shall nevertheless have in respect of such breach the rights and remedies provided by the following provisions of this Article VIII if, but only if, Parent has delivered an Indemnification Notice with respect to such breach before the Expiration Date. Any claim of breach of a covenant or agreement contained herein that contemplates performance prior to the Closing Date not set forth in reasonable detail (based on the factual information then reasonably available to the claimant) by
written notice to the party who is claimed to have breached such covenant or agreement before the expiration of the period for assertion of such claims provided by the immediately preceding sentence is hereby barred, may not be pursued and is hereby irrevocably waived as of the expiration of such period.

SECTION 8.2 Indemnification.

(a) Right to Indemnity. The Company Unitholders, to the extent (and only to such extent) and in the manner hereinafter provided, shall indemnify and hold harmless Parent, the Acquiring Corp., the Surviving Company and their respective subsidiaries, and the directors, officers, employees, consultants, attorneys, agents and representatives thereof (the "Parent Indemnified Parties") from and against any and all Losses (irrespective of whether or not such Losses arise out of or in connection with a third party claim) to the extent, but only to the extent, resulting from, arising out of or otherwise relating to:

(i) any failure of the representations and warranties made by the Company set forth in this Agreement or in any Company Document to be true and correct (without regard to any notice given by the Company in accordance with clause (iii) of the first sentence of Section 5.6);

(ii) any breach of any covenant or other agreement required by this Agreement to be performed by the Company prior to the Closing, or

(iii) any Tax Losses,

such Losses collectively being referred to herein as "Parent Indemnifiable Losses." provided, however, that (i) the Parent Indemnified Parties may not recover any amount for Parent Indemnifiable Losses, unless and until the aggregate amount of all Parent Indemnifiable Losses, other than Tax Losses, exceeds $500,000 (the "Deductible"), with any Tax Losses not being subject to any Deductible, and then only with respect to such amounts of Parent Indemnifiable Losses, other than Tax Losses, in excess of the Deductible, (ii) the maximum amount of indemnity that all Parent Indemnified Parties shall be entitled to for all claims of indemnity hereunder shall not exceed $35,000,000, and (iii) the Parent Indemnified Parties may not recover any amount for Parent Indemnifiable Losses from the Working Capital Payment described in Section 2.2(g) herein. For purposes of applying the indemnification provisions of this Article VIII, in determining whether a representation, warranty, covenant or agreement referred to in Section 8.2(a) or (b) had been breached or violated, and in calculating the Losses sustained by reason of a breach or failure by the Company referred to in Section 8.2(a) or (b), any materiality (including Material Adverse Effect) qualifications in the representations, warranties, covenants and agreements so breached or violated shall be ignored.

(b) Tax Losses. For purposes of Section 8.2(a), "Tax Losses" means any and all Losses attributable to (1) Taxes (or the non-payment thereof) of the Company.
or its Subsidiaries for all Pre-Closing Tax Periods (including the portion of any Straddle Period attributable to the Pre-Closing Tax Period and including any Taxes arising by reason of the transactions contemplated hereby) or to the Closing itself and (2) Taxes against which Parent shall be entitled to indemnity under the Subscription Agreements.

(c) Sources of Indemnity Payments. Subject to the following provisions of this Article VIII, reduction of the Deferred Payment (or a disbursement to Parent from the Escrow Account, if the Escrow Account shall have been established) shall be the source for funding any indemnity payment due to a Parent Indemnified Party hereunder, but to the extent the amount of the Deferred Payment (or amount in the Escrow Account) is not sufficient therefor, the Parent may, in its discretion, reduce the amount of the cash to be included in a payment of Earn-out Consideration it expects to make by the amount equal to the amount due to a Parent Indemnified Party as indemnity hereunder and not satisfied by reduction of the Deferred Payment (or a disbursement to Parent from the Escrow Account) and, to the extent the amount so due to a Parent Indemnified Party is not so satisfied, then the Unitholder Representative shall be required to pay all of such additional sums due and owing to the Parent Indemnified Party by transfer of immediately available funds within thirty (30) days after the date of notice. To the extent any amount is due to a Parent Indemnified Party other than Parent pursuant to this Article VIII, Parent shall seek recovery of such amount on behalf of the Parent Indemnified Party (and is hereby authorized to act on behalf of such Parent Indemnified Party for such purpose) by a reduction of the Deferred Payment or by a disbursement from the Escrow Account in an amount equal to the amount due to such Parent Indemnified Party, and Parent, upon recovery thereof, shall promptly pay the amount thereof over to such Parent Indemnified Party, provided, however, to the extent the amount so due to such Parent Indemnified Party is not satisfied by reduction of the Deferred Payment or a disbursement from the Escrow Account, the Unitholder Representative shall be required to pay all of such additional sums due and owing to such Parent Indemnified Party by transfer of immediately available funds within thirty (30) days after the date of notice of any sums then due and owing is given to the Unitholder Representative by the Parent Indemnified Party. If the Unitholder Representative shall have disputed the making of an indemnification payment to Parent by reduction of the Deferred Amount, or a disbursement from the Escrow Account, as provided by Section 8.4(c) and such payment remains in dispute at such time as Parent is required to make a payment of Earn-out Consideration, as provided by Section 2.1(c), then Parent may, in its discretion, make such payment of Earn-out Consideration, to the extent of all or part of the amount of the indemnification payment so disputed, into the Escrow Account (if then in existence) or into an escrow account to be established on substantially the same terms as provided for the funding of the Deferred Payment amount into escrow by Section 2.2(a). In such event, upon resolution of such dispute as provided by Section 8.3(c), the entire amount so deposited in escrow (and any net earnings thereon) shall be disbursed out of escrow either to Parent in payment of such indemnification or to the Unitholder Representative (for the benefit of Company Unitholders), as appropriate depending on the resolution of such dispute, the amount of the indemnity payment, if any, to be made by to Parent and the amount of Earn-out Consideration so withheld. The

59
Unitholder Representative shall be entitled to seek reimbursement or contribution from each other Company Unitholder, in accordance with such agreement as may exist between the Unitholder Representative and such Company Unitholder or as permitted by law, for the pro rata portion of any such indemnity payment made by the Unitholder Representative determined by the ratio of the amount of Merger Consideration received by such Company Unitholder in relation to the total amount of Merger Consideration paid by Parent, in each case to the date the Unitholder Representative made such indemnity payment.

SECTION 8.3 Indemnification Procedures.

(a) Indemnification Notices. In order to obtain indemnity in respect of a Loss as provided by Section 8.2, a Parent Indemnified Party shall give an “Indemnification Notice” to the Unitholder Representative. For the purposes hereof, an “Indemnification Notice” shall mean a notice signed by any officer of Parent and delivered to the Unitholder Representative and (i) stating that Parent has paid, incurred, sustained or accrued, or reasonably anticipates that it will be obligated to pay, incur, sustain or accrue, a Loss against which it is entitled to indemnity, (ii) specifying in reasonable detail the nature of such Loss (including the calculation thereof or the basis for estimation thereof), the date insofar as practicable such Loss was paid or is expected to be incurred, sustained or accrued or the basis on which it anticipates incurring, sustaining or accruing such Loss, and the nature of the misrepresentation, breach of warranty or covenant resulting in such Loss or out of which such Loss arose or to which such Loss relates or the nature of the Tax Loss, and (iii) the amount of cash to be delivered to Parent (for the benefit of the pertinent Parent Indemnified Party) as indemnity against each such Loss. If a Loss is anticipated but not yet incurred, sustained or accrued at the time an Indemnification Notice is given, an additional Indemnification Notice shall be given providing such information regarding the Loss incurred, sustained or accrued as was not included in an earlier Indemnification Notice. In a case where a Parent Indemnified Party other than Parent shall seek to obtain the indemnity provided by Section 8.2, Parent shall give an appropriate Indemnification Notice on behalf of such Parent Indemnified Party, provided that such Parent Indemnified Party has provided to Parent such information as Parent may reasonably request for such purpose.

(b) Third-Party Claims. A Parent Indemnified Party shall give the Unitholder Representative written notice (which may be part of an Indemnification Notice) of any claim, assertion or action by or in respect of a third party, including any civil, criminal, administrative, regulatory, investigative or arbitral proceeding, as to which such Parent Indemnified Party may request indemnification hereunder or as to which the Deductible may be applied as soon as is practicable and in any event within fifteen calendar days of the time that such Parent Indemnified Party learns of such claim, assertion, action or proceeding; provided, however, that the failure to so notify the Unitholder Representative shall not affect the rights of the Parent Indemnified Party to indemnification hereunder except to the extent that the Unitholder Representative (as such) is prejudiced by such failure. Parent (on its own behalf or on behalf of any other Parent Indemnified Party if such claim, assertion, action or proceeding involves another
Parent Indemnified Party) shall direct, through counsel of its own choosing reasonably acceptable to the Unitholder Representative, the response to, defense of or settlement of any such claim, assertion, action or proceeding, but the cost thereof shall be an indemnifiable Loss in accordance with Section 8.2. Parent shall consult with the Unitholder Representative for the purpose of allowing the Unitholder Representative to participate in responding to, defending or settlement of claim, assertion, action or proceeding, but in such case the expenses of the Unitholder Representative, including the fees and disbursements of its counsel, shall be paid by the Unitholder Representative. Parent shall provide and shall cause the Surviving Company to provide (during normal business hours) the Unitholder Representative and its counsel with reasonable access to the records and personnel of the Surviving Company and Parent relating to any claim, assertion, action or proceeding subject to indemnity hereunder during normal business hours. If the Unitholder Representative shall determine to be represented by counsel in any such proceeding, Parent shall cooperate, and cause the counsel representing it in such proceeding to cooperate, with counsel representing the Unitholder Representative in such proceeding. Parent shall not pay, or permit to be paid, any part of any third party claim or demand in respect of which indemnification has been sought hereunder unless the Unitholder Representative consents in writing to such payment (which consent shall not be unreasonably withheld) or unless a final judgment from which no appeal may be taken by or on behalf of the Unitholder Representative is entered against the Parent Indemnified Party for such liability or unless, upon request of Parent, the Unitholder Representative has failed to show to Parent’s reasonable satisfaction that, taking into account the then amount of the Deferred Payment and any Earn-out Consideration anticipated to be payable by Parent, there are not readily available to the Unitholder Representative sufficient funds to pay the amount in respect of such claim, demand or proceeding for which an Indemnification Notice has been given. If the Unitholder Representative deposits with Parent an irrevocable letter of credit, or similar form of financial assurance, in the amount for which the Indemnification Notice has been given by Parent in connection with such third-party proceeding, the Unitholder Representative shall be considered to have shown that there are readily available sufficient funds to pay such amount.

(c) Resolution of Conflicts; Arbitration.

(i) If the Unitholder Representative shall object in writing to any claim or claims for indemnification made in any Indemnification Notice within thirty (30) days after delivery of such Indemnification Notice, then the Unitholder Representative and Parent shall attempt in good faith to agree upon the rights of the respective parties with respect to each of such claims. If the Unitholder Representative and Parent should so agree, a memorandum setting forth such agreement shall be prepared and signed by both parties and the Parent shall be entitled to rely on any such memorandum and withhold payment to the Company Unitholders from the Deferred Payment in accordance with the terms thereof.

(ii) If no such agreement can be reached after good faith negotiation within sixty (60) days after delivery of an Indemnification Notice,
either Parent or the Unitholder Representative may demand arbitration of the matter in accordance with the following provisions of this Section 8.3 unless the amount of the Loss is at issue in pending litigation with a third party, in which event arbitration shall not be commenced until such amount is ascertained or both parties agree to arbitration. If such dispute is subject to arbitration, it shall be settled by arbitration conducted in accordance with the rules and procedures then in effect of the American Arbitration Association by one arbitrator mutually agreeable to Parent and the Unitholder Representative. In the event that, within thirty (30) days after submission of any dispute to arbitration, Parent and the Unitholder Representative cannot mutually agree on one arbitrator, then, within fifteen (15) days after the end of such thirty (30)-day period, Parent and the Unitholder Representative shall each select one arbitrator. The two arbitrators so selected shall select a third arbitrator. If one party but not the other fails to select an arbitrator during this fifteen (15)-day period, then the parties agree that the arbitration will be conducted by the one arbitrator selected by the party which has made such a selection.

(iii) Any such arbitration shall be held in New York, New York. The arbitrator(s) shall determine how all expenses relating to the arbitration shall be paid, including the respective expenses of each party, the fees of each arbitrator and the administrative fee of the American Arbitration Association. The arbitrator or arbitrators, as the case may be, shall set a limited time period and establish procedures designed to reduce the cost and time for discovery while allowing the parties an opportunity, adequate in the sole judgment of the arbitrator or majority of the three arbitrators, as the case may be, to discover relevant information from the opposing parties about the subject matter of the dispute. The arbitrator, or a majority of the three arbitrators, as the case may be, shall rule upon motions to compel or limit discovery and shall have the authority to impose sanctions, including attorneys’ fees and costs, to the same extent as a competent court of law or equity, should the arbitrators or a majority of the three arbitrators, as the case may be, determine that discovery was sought without substantial justification or that discovery was refused or objected to without substantial justification. The decision of the arbitrator or a majority of the three arbitrators, as the case may be, as to the validity and amount of any claim for indemnification made in an Indemnification Notice shall be final, binding, and conclusive upon the parties to this Agreement. Such decision shall be written and shall be supported by written findings of fact and conclusions which shall set forth the award, judgment, decree or order awarded by the arbitrator(s). In accordance with the provisions of this Agreement, the Company shall be entitled to rely on, and to reduce the amount of the Deferred Payment in accordance with, the terms of such award, judgment, decree or order, as applicable. Within ten (10) days of a decision of the arbitrator(s) requiring payment by one party to another, such party shall make the payment to such other party. Judgment upon any award rendered by the arbitrator(s) may be entered in any court having jurisdiction.
SECTION 8.4 Reduction of the Deferred Payment Amount.

(a) Until payable to the Company Unitholders as provided in accordance with Section 2.2(a), the Deferred Payment shall be reduced to compensate the Parent Indemnified Parties for any Losses incurred or sustained by them and against which they are entitled to indemnity under this Article VIII; provided, however, that Acquiring Corp. shall not be required to pay the Deferred Payment to the Company Unitholders when otherwise due hereunder in accordance with Section 2.1(a) with respect to the portion of the amount of the Deferred Payment equal to 120% of the aggregate amount of any then unresolved indemnity claims specified in any Indemnification Notice or Indemnification Notices delivered in good faith to the Company prior to the time the Deferred Payment is otherwise payable in accordance with Section 2.1(a)(each, an “Unresolved Claim”). As soon as all Unresolved Claims have been resolved, Parent shall deliver to the Company Unitholders (as such immediately before the Closing as contemplated by Section 2.1(a)) the remaining amount of the Deferred Payment, if any, not applied to satisfy Unresolved Claims.

(b) Claims for Reduction of the Deferred Payment. Parent shall be entitled to reduce the amount of the Deferred Payment by an amount equal to the amount of the indemnity payment stated in the Indemnification Notice to be made in respect the Losses described in the Indemnification Notice; provided, however, that, to the extent the Indemnification Notice states only the basis for anticipated Losses, the Deferred Payment shall not be so reduced until such Losses are actually paid, incurred or sustained as specified in a further Indemnification Notice. If the Unitholder Representative does not object to an Indemnification Notice in writing within the 30-day period set forth in Section 8.4(c) after delivery by Parent of an Indemnification Notice, such failure to so object shall constitute an irrevocable acknowledgment by the Unitholder Representative, on behalf of all holders of Company Units, that the Parent Indemnified Party is entitled to the full amount of the claim for Losses set forth in such Indemnification Notice; provided, however, that to the extent an Indemnification Notice states only the basis for anticipated Losses, no amount shall be distributed until such Losses are actually paid, incurred or sustained (notwithstanding the Unitholder Representative’s failure to object in writing).

(c) Objections to Claims against the Deferred Payment. At the time of delivery of any Indemnification Notice to Unitholder Representative, and for a period of thirty days after such delivery Parent shall make no reduction in the Deferred Amount pursuant to Section 8.3(b) unless the Parent shall have received written authorization from the Unitholder Representative to make such delivery. After the expiration of such 30-day period, Parent shall be entitled to reduce the Deferred Payment to satisfy such
claims pursuant to Section 8.3(b), provided that no deduction shall be made if the Unitholder Representative shall object in a written statement to the claim made in the Indemnification Notice, and such statement shall have been delivered to Parent prior to the expiration of such 30-day period.

SECTION 8.5 Exclusivity of Remedy. From and after the Effective Time, except in respect of fraudulent conduct, indemnity in accordance with the provisions of this Article VIII shall be the sole and exclusive remedy of Parent and Parent shall have no other right to pursue any Company Unitholder for any liability for breach of any representation, warranty, covenant or agreement of the Company contained herein or in any document delivered as provided hereby.

SECTION 8.6 Tax Treatment of Indemnity Payments. The Company and the Company Unitholders and Parent agree to treat any indemnity payment made pursuant to this Article VIII as an adjustment to the Merger Consideration for federal, state, local and foreign income tax purposes unless a contrary treatment is required under applicable Law.

ARTICLE IX
Miscellaneous

SECTION 9.1 Unitholder Representative.

(a) Raju Mantena shall represent and act as agent for all the other Company Unitholders for the purposes specified in this Agreement. As Unitholder Representative, he shall be authorized and empowered, as agent of and on behalf of all Company Unitholders entitled to receive any consideration pursuant to this Agreement by reason of the Merger or otherwise having an interest in any matter concerning this Agreement, to give and receive notices and communications as provided herein, to determine the Earn-out Percentages, to object to any claim for indemnification made by any Parent Indemnified Party, to negotiate, agree to, enter into and perform (including giving any notice or instructions relating to any escrow arrangement contemplated hereby) any agreement, instrument or other document contemplated hereby to be entered into by the Company or the Company Unitholders or in the Unitholder’s judgment necessary or appropriate to the performance thereof, to agree to, negotiate, enter into settlements and compromises of, and demand arbitration and comply with orders of courts and awards of arbitrators with respect to such claims or proceedings in respect of which such an indemnity claim is made hereunder, to receive payments on behalf of the Company Unitholders due and owing pursuant to this Agreement (including by reduction of the Deferred Payment) and acknowledge receipt of payments due to the Company or any Company Unitholder hereunder, to waive before or after the Effective Time any breach or default of Parent, Acquiring Corp. or Merger Sub of any obligation to be performed by it under this Agreement, to receive service of process on behalf of each Company Unitholder in connection with any claims against such Company Unitholder arising under or in connection with this Agreement, any document or instrument provided for hereby or any of the Transactions, and to take all other actions that are either (i)
necessary or appropriate in the judgment of the Unitholder Representative for the accomplishment of the foregoing or (ii) specifically mandated by the terms of this Agreement. In the event of the death or disability or resignation of the initial Unitholder Representative, a substitute shall be appointed by the holders of a majority in interest of the Units by a writing delivered to Parent (and shall thereupon be the “Unitholder Representative.”) No bond shall be required of the Unitholder Representative, and the Unitholder Representative shall not receive any compensation for its services. Notices or communications to or from the Unitholder Representative shall constitute notice to or from the Company Unitholders.

(b) In dealing with this Agreement and any notice, instrument, agreement or document relating thereto, and in exercising or failing to exercise all or any of the powers conferred upon the Unitholder Representative hereunder or thereunder, (i) the Unitholder Representative and its agents, counsel, accountants and other representatives shall not assume any, and shall incur no, responsibility whatsoever (in each case, to the extent permitted by applicable Law) to the Company Unitholders, Parent or the Surviving company by reason of any error in judgment or other act or omission performed or omitted hereunder or in connection with this Agreement or any such other agreement, instrument or document, other than in respect of an act or omission done in bad faith or with gross negligence on the part of the Unitholder Representative, and (ii) the Unitholder Representative shall be entitled to rely in good faith on the advice of counsel, public accountants or other independent experts experienced in the matter at issue, and any error in judgment or other act or omission of the Unitholder Representative pursuant to such advice shall in no event subject the Unitholder Representative to liability to the Company Unitholders, Parent or the Surviving company. Pursuant to the following sentence, and to the fullest extent permitted by applicable Law, the Company Unitholders shall be, severally based on each Company Unitholder’s pro rata share of the Merger Consideration and not jointly, obligated to indemnify the Unitholder Representative and hold the Unitholder Representative harmless against any loss, liability or expense incurred without gross negligence or bad faith on the part of the Unitholder Representative arising out of or in connection with the acceptance or administration of the Unitholder Representative’s duties hereunder, including the reasonable fees and expenses of any legal counsel retained by the Unitholder Representative.

(c) The grant of authority provided for in this Section 9.1: (i) is coupled with an interest and is being granted, in part, as an inducement to Parent and Merger Sub to enter into this Agreement, and shall be irrevocable and survive the dissolution, liquidation or bankruptcy of the Company or the death, incompetency, liquidation or bankruptcy of any Company Unitholder, shall be binding on any successor thereto, and (ii) shall survive the delivery of an assignment by any Company Unitholder of the whole or any fraction of his, her or its interest in the Deferred Payment.

(d) In connection with the performance of his obligations hereunder, the Unitholder Representative shall have the right at any time and from time to time to select and engage, at the cost and expense of the Company Unitholders (as contemplated by Section 9.1(b)), attorneys, accountants, investment bankers, advisors, consultants and
clerical personnel and obtain such other professional and expert assistance, and maintain such records, as the Unitholder Representative may deem necessary or desirable and incur other out-of-pocket expenses related to performing its services hereunder.

(c) All of the immunities and powers granted to the Unitholder Representative under this Agreement shall survive the Closing and/or any termination of this Agreement.

(f) A decision, act, consent or instruction of the Unitholder Representative, including an extension or waiver of this Agreement pursuant to Article VII or Section 9.3, as applicable, shall constitute a decision of the Company Unitholders and shall be final, binding and conclusive upon the Company Unitholders; Parent and the Surviving company may rely upon any such decision, act, consent or instruction of the Unitholder Representative as being the decision, act, consent or instruction of all the Company Unitholders. Parent and the Surviving company are hereby relieved from any Liability to any Person for any acts done by them in accordance with such decision, act, consent or instruction of the Unitholder Representative.

(g) The Unitholder Representative has all requisite power, authority and legal capacity to execute and deliver this Agreement and each other agreement, document, or instrument or certificate contemplated by this Agreement or to be executed by the Unitholder Representative in connection with the consummation of the transactions contemplated by this Agreement (together with this Agreement, the “Unitholder Representative Documents”), and to consummate the transactions contemplated hereby and thereby. The execution and delivery of this Agreement and each of the Unitholder Representative Documents, the performance of its respective obligations hereunder and thereunder and the consummation of the transactions contemplated hereby and thereby have been duly authorized by all required action on the part of the Unitholder Representative. This Agreement has been, and each of the Unitholder Representative Documents will be at or prior to the Closing, duly and validly executed and delivered by the Unitholder Representative and (assuming the due authorization, execution and delivery by the other parties hereto and thereto) this Agreement constitutes, and each of the Unitholder Representative Documents when so executed and delivered will constitute, legal, valid and binding obligations of the Unitholder Representative enforceable against it in accordance with their respective terms, subject to applicable bankruptcy, insolvency, reorganization, moratorium and similar laws affecting creditors’ rights and remedies generally, and subject, as to enforceability, to general principles of equity, including principles of commercial reasonableness, good faith and fair dealing (regardless of whether enforcement is sought in a proceeding at law or in equity).

(h) Each of the Company Unitholders hereby agrees to the foregoing provisions of this Section 9.1 and shall become parties to the Merger Agreement for purposes of such Section.
SECTION 9.2 Amendment or Supplement. At any time prior to the Effective Time, this Agreement may be amended or supplemented in any and all respects, by written agreement of the parties hereto, authorized by action taken by their respective Boards of Directors or equivalent body; provided, however, that no amendment or change to the provisions hereof shall be made which by Law would require further approval by the Company Unitholders without such approval.

SECTION 9.3 Extension of Time, Waiver, Etc. At any time prior to the Effective Time, any party may, subject to Section 9.2 and applicable Law, (a) waive any inaccuracies in the representations and warranties of any other party hereto, (b) extend the time for the performance of any of the obligations or acts of any other party hereto or (c) waive compliance by the other party with any of the agreements contained herein or, except as otherwise provided herein, waive any of such party’s conditions. Notwithstanding the foregoing, no failure or delay by the Company, Parent or Merger Sub in exercising any right hereunder shall operate as a waiver thereof nor shall any single or partial exercise thereof preclude any other or further exercise thereof or the exercise of any other right hereunder. Any agreement on the part of a party hereto to any such extension or waiver shall be valid only if set forth in an instrument in writing signed on behalf of such party.

SECTION 9.4 Assignment. Neither this Agreement nor any of the rights, interests or obligations hereunder shall be assigned, in whole or in part, by operation of Law or otherwise, by any of the parties without the prior written consent of the other parties, except that Merger Sub may assign, in its sole discretion, any or all its rights, interests and obligations under this Agreement to any wholly owned Subsidiary of Parent, but no such assignment shall relieve Merger Sub of any of its obligations hereunder. Subject to the preceding sentence, this Agreement shall be binding upon, inure to the benefit of, and be enforceable by, the parties hereto and their respective successors and permitted assigns. Any purported assignment not permitted under this Section shall be null and void.

SECTION 9.5 Counterparts. This Agreement may be executed in counterparts (each of which shall be deemed to be an original but all of which taken together shall constitute one and the same agreement) and shall become effective when one or more counterparts have been signed by each of the parties and delivered to the other parties.

SECTION 9.6 Entire Agreement; No Third-Party Beneficiaries. This Agreement, the Company Disclosure Schedule and the Confidentiality Agreement (a) constitute the entire agreement, and supersede all other prior agreements and understandings, both written and oral, among the parties, or any of them, with respect to the subject matter hereof and thereof and (b) except for the provisions of Section 5.8 and Article VIII, are not intended to and shall not confer upon any Person other than the parties hereto any rights or remedies hereunder.
SECTION 9.7 Governing Law; Jurisdiction; Waiver of Jury Trial

(a) This Agreement shall be governed by, and construed in accordance with, the laws of the State of Delaware without regard to the principles, policies or provisions thereof concerning conflict or choice of laws.

(b) Each of the parties hereto hereby irrevocably waives any and all rights to trial by jury in any legal proceeding arising out of or related to this Agreement or the Transactions.

SECTION 9.8 Specific Enforcement. The Company, Parent and Merger Sub agree that irreparable damage would occur in the event that any of the provisions of this Agreement were not performed in accordance with their specific terms or were otherwise breached. It is accordingly agreed that the Company, Parent and Merger Sub shall be entitled to an injunction or injunctions to prevent breaches of this Agreement and to enforce specifically the terms and provisions of this Agreement in any Delaware state court or any federal court of competent jurisdiction, without any bond or other security being required of it therefor, this being in addition to any other remedy to which they are entitled at law or in equity.

SECTION 9.9 Consent to Jurisdiction. Each of the parties hereto (i) consents to submit itself to the personal jurisdiction of any Delaware state court or any federal court located in the State of Delaware with respect to any action or proceeding arising out of any dispute pertaining to this Agreement or any of the Transactions, (ii) agrees that it will not attempt to deny or defeat such personal jurisdiction by motion or other request for leave from any such court and (iii) agrees that it will not bring any action relating to this Agreement or any of the Transactions in any other court (and any appropriate court for the prosecution of any appeal from or against any decision or action thereof).

SECTION 9.10 Notices. All notices, requests and other communications to any party hereunder shall be in writing and shall be deemed given if delivered personally, sent by facsimile (receipt of which is confirmed) or sent by overnight courier (providing proof of delivery) to the parties at the following addresses:

If to Parent, Acquiring Corp. or Merger Sub, to:

Magellan Health Services, Inc.
55 Nod Road
Avon, Connecticut 06001
Attention: Daniel Gregoire, General Counsel
Facsimile: (860) 507-1990
with a copy (which shall not constitute notice) to:

Weil, Gotshal & Manges LLP
767 Fifth Avenue
New York, NY 10153
Attention: Robert L. Messineo
Facsimile: (212) 310-8007

If to the Company, to:

5850 T.G. Lee Blvd., Suite 510
Orlando, FL 32822
Attention: Raju Mantena
Facsimile: (866) 994-2673

with a copy (which shall not constitute notice) to:

Akerman Senterfitt
One SE Third Avenue, 28th Floor
Miami, FL 33131
Attention: Marshall R. Burack
Facsimile: (305) 374-5095

or such other address or facsimile number as such party may hereafter specify by like notice to the other parties hereto. All such notices, requests and other communications shall be deemed received on the date of receipt by the recipient thereof if received prior to 5 P.M. in the place of receipt and such day is a business day in the place of receipt. Otherwise, any such notice, request or communication shall be deemed not to have been received until the next succeeding business day in the place of receipt.

SECTION 9.11 Severability. If any term or other provision of this Agreement is determined by a court of competent jurisdiction to be invalid, illegal or incapable of being enforced by any rule of law or public policy, all other terms, provisions and conditions of this Agreement shall nevertheless remain in full force and effect. Upon such determination that any term or other provision is invalid, illegal or incapable of being enforced, the parties hereto shall negotiate in good faith to modify this Agreement, to the fullest extent permitted by applicable law, so as to effect the original intent of the parties as closely as possible, to the end that the transactions contemplated hereby may, except in respect of such modified provision, be consummated as contemplated hereby.

SECTION 9.12 Definitions.

(a) As used in this Agreement, the following terms have the meanings ascribed thereto below:
“Affiliate” shall mean, as to any Person, any other Person that, directly or indirectly, controls, or is controlled by, or is under common control with, such Person. For this purpose, “control” (including, the correlative terms, “controlled by” and “under common control with”) shall mean the possession, directly or indirectly, of the power to direct or cause the direction of management or policies of a Person, whether through the ownership of securities or partnership or other ownership interests, by contract or otherwise.

“business day” shall mean a day except a Saturday, a Sunday or other day on which the SEC or banks in the City of New York are authorized or required by Law to be closed.

“Change of Control” shall mean the occurrence of (1) any of the following transactions:

(i) any “person,” as such term is used in Sections 13(d) and 14(d) of the Exchange Act of 1934 (other than the Parent, any trustee or other fiduciary holding securities under any employee benefit plan of the Parent, or any company owned, directly or indirectly, by the stockholders of the Parent in substantially the same proportions as their ownership of common stock of Parent at such time or immediately before such company came to own securities of Parent), is or becomes the “beneficial owner” (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of Parent representing fifty percent (50%) or more of the combined voting power in the election of directors of Parent’s then outstanding securities,

(ii) during any period of two consecutive years, individuals who at the beginning of such period constitute the Board of Directors of Parent, and any new director (other than a director designated by a person who has entered into an agreement with Parent to effect a transaction described in clause (1)(i), (iii), or (iv) of this paragraph) whose election by such Board or nomination for election by Parent’s stockholders was approved by a vote of at least a majority of the directors of Parent then still in office who either were directors at the beginning of the two-year period or whose election or nomination for election was previously so approved, cease for any reason to constitute at least a majority of the Board,

(iii) a merger or consolidation of Parent with any other corporation, other than a merger or consolidation which would result in the voting securities of Parent outstanding immediately prior thereto continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity) more than fifty percent (50%) of the combined voting power of the voting securities of Parent or such surviving entity outstanding immediately after such merger or consolidation, or
the stockholders of Parent approve a plan of complete liquidation of Parent or the consummation of the sale or disposition by Parent of all or substantially all of the Parent’s assets other than (x) the sale or disposition of all or substantially all of the assets of Parent to a person or persons who beneficially own, directly or indirectly, at least fifty percent (50%) or more of the combined voting power of the outstanding voting securities of Parent at the time of the sale or (y) pursuant to a spin-off type transaction, directly or indirectly, of such assets to the stockholders of Parent.

and (2) as a result of such transaction Parent either (x) shall come to be controlled by a company that is not primarily engaged in the business of investing or (y) shall come to be controlled by a company that is primarily engaged in the business of investing and two of the three senior executive officers of Parent in office immediately before such transaction occurs shall within 120 days after such transaction occurs cease to be a senior executive officer of the Parent (or its successor company pursuant to such transaction). For purposes hereof, the “senior executive officers” of Parent shall mean the chief executive officer, the chief operating officer and the chief financial officer.

“Company Documents” shall mean each agreement, document or instrument or certificate contemplated by this Agreement or to be executed by the Company or its Subsidiaries in connection with the transactions contemplated by this Agreement (including, without limitation, the Company Disclosure Schedules).

“Credit Agreement” with respect to Parent shall mean the Credit Agreement, dated as of January 5, 2004, among Parent, various lenders and Deutsche Bank AG, New York Branch, as Administrative Agent, as amended and in effect on the date hereof and as the same may be amended from time to time or replaced by any comparable agreement.


“Fair Market Value” shall mean, with respect to Parent Shares, as of any date the average over the period of twenty (20) trading days preceding that date of the closing trading prices of the Ordinary Common Stock of Parent in trading on The Nasdaq Stock Market.

“First-Earn-out Distribution Date” shall mean the date selected by Parent which is within five business days following the date on which Parent’s earnings for year ended December 31, 2007 shall have first been publicly disclosed by Parent.

“GAAP” shall mean generally accepted accounting principles in the United States as of the date hereof.

“Governmental Authority” shall mean any government, court, regulatory or administrative agency, commission or authority or other governmental instrumentality, federal, state or local, domestic, foreign or multinational.
“Healthcare Laws” means any Law relating to the provision, administration, and/or payment for healthcare or healthcare-related products or services, including, without limitation, to the extent applicable: (i) rules and regulations governing the operation and administration of Medicare, Medicaid, or other federal and state health care programs; (ii) 42 U.S.C. § 1320a-7(b), commonly referred to as the “Federal Anti-Kickback Statute,” (iii) 42 U.S.C. § 1395nn, commonly referred to as the “Stark Law,” (iv) 31 U.S.C. §§ 3729 et seq., commonly referred to as the “False Claims Act,” (v) 31 U.S.C. § 3801 et seq., commonly referred to as the Program Fraud Civil Penalties Act, (vi) the rules and regulations of the U.S. Food and Drug Administration, and (vii) rules and regulations of the state boards of pharmacy.

“HSR Act” shall mean the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended.

“Knowledge” in the case of an individual shall mean, with respect to any matter, the actual knowledge of such Person after due inquiry about the matter and, in the case of the Company, shall mean the Knowledge of the individuals identified on Schedule 3.25, and, in the case of Parent or Merger Sub, the Knowledge of any of the chief executive officer, the chief operating officer, the chief financial officer, the chief accounting officer and the General Counsel of Parent. For purposes hereof, “due inquiry” shall mean such inquiry as is reasonable under the circumstances in accordance with good business practices for an individual in a like position of responsibility with respect to a business of like size and nature when addressing a matter of importance to such business.

“Liability” means any debt, loss, damage, obligation, adverse claim or other liability (whether direct or indirect, known or unknown, asserted or unasserted, absolute or contingent, accrued or unaccrued, liquidated or unliquidated, or due or to become due, and whether in contract, tort, strict liability or otherwise).

“Liens” shall mean any lien, pledge, mortgage, encumbrance, security interest of any kind, charge or adverse right of any kind or nature whatsoever (including any restriction on the right to vote or transfer and securities, except for such transfer restrictions of general applicability as may be provided under the Securities Act of 1933, as amended, and the rules and regulations promulgated thereunder, and the “blue sky” laws of the various States of the United States).

“Losses” shall mean with regard to any breach or violation of a representation or warranty or covenant or any third-party claim or investigation or other matter in respect of which a person is entitled to indemnity hereunder any out-of-pocket cost or expense (including attorneys fees and disbursements reasonably incurred and court costs), any monetary damages, fines or penalties, and any losses or other Liabilities sustained by such person (including as a consequence of any injunction issued or other equitable relief granted against such person) as a result of or in connection with such matter.
“Magellan Cash Investment Rate” shall mean the annual rate of return equal to the rate of return from time to time earned by Parent and its Subsidiaries on all of their cash investments (including restricted accounts) in the aggregate, determined on a quarterly basis for each fiscal quarter commencing with the fiscal quarter in which the Closing occurs and continuing until the fiscal quarter ended before the last disbursement of the Deferred Payment as provided hereby, as determined by Parent in the ordinary course of business consistent with the accounting practices used in the preparation of its consolidated financial statements filed under the Exchange Act.

“Material Adverse Effect” shall mean with respect to the Company or Parent, an event, change in circumstance or state of facts which has, or would reasonably be expected at any time within the two year period following the occurrence of such event, change of circumstance or state of facts to have, a material adverse effect on the business, properties, assets, liabilities (contingent or otherwise), results of operations or condition (financial or otherwise) of the Company or Parent, as the case may be (considered together with its Subsidiaries as a whole), except for any such effects resulting from (i) the negotiation, execution, announcement or performance of this Agreement or the consummation of the transactions contemplated by this Agreement, including the impact thereof on relationships, contractual or otherwise, with customers, suppliers, licensors, distributors, partners or employees, (ii) changes in general economic or political conditions or the securities markets in general (whether as a result of acts or terrorism, war (whether or not declared), armed conflicts or otherwise) or (iii) changes in conditions generally applicable to businesses in the same or similar industries of such Person including, without limitation, (A) changes in laws, regulations, rules, ordinances, policies, mandates, guidelines or other requirements of any Governmental Authority generally applicable to such businesses or industries or (B) changes in generally accepted accounting principles as applied in the United States on a consistent basis or its application.

“ordinary course of business” means the ordinary and usual course of day-to-day operations of the business of the Company and its Subsidiaries through the date hereof consistent with past practice.

“Percentage Interest” shall have the meaning ascribed to it under the operating agreement of the Company, as amended to the date hereof.

“Person” shall mean an individual, a corporation, a limited liability company, a partnership, an association, a trust or any other entity, including a Governmental Authority.

“Pre-Closing Tax Period” means any taxable period ending on or before the Closing Date.

“Second Earn-out Distribution Date” shall mean the date selected by Parent which is within five business days following the date on which Parent’s earnings for the year ended December 31, 2008 shall have first been publicly disclosed by Parent.
“Straddle Period” means any taxable period beginning on or prior to and ending after the Closing Date.

“Subsidiary” when used with respect to any party, shall mean any corporation, limited liability company, partnership, association, trust or other entity the accounts of which would be consolidated with those of such party in such party’s consolidated financial statements if such financial statements were prepared in accordance with GAAP, as well as (except where reference is made to the party’s financial statements) any other corporation, limited liability company, partnership, association, trust or other entity of which securities or other ownership interests representing more than 50% of the equity or more than 50% of the ordinary voting power (or, in the case of a partnership, more than 50% of the general partner interests) are, as of such date, owned by such party or one or more Subsidiaries of such party or by such party and one or more Subsidiaries of such party.

“Target Percentage Interest” shall have the meaning ascribed to it under the operating agreement of the Company, as amended to the date hereof.

“Taxing Authority” means the IRS and any other Governmental Authority responsible for the administration of any Tax.

“Transactions” refers collectively to the transactions provided by this Agreement to be consummated by the parties hereto, including the Merger and the payment of the Merger Consideration.
The following terms are defined on the page of this Agreement set forth after such term below:

<table>
<thead>
<tr>
<th>Term</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agreement</td>
<td>1</td>
</tr>
<tr>
<td>Allocation Schedule</td>
<td>47</td>
</tr>
<tr>
<td>Antitrust Laws</td>
<td>44</td>
</tr>
<tr>
<td>Balance Sheet</td>
<td>16</td>
</tr>
<tr>
<td>Balance Sheet Date</td>
<td>16</td>
</tr>
<tr>
<td>Bankruptcy and Equity Exception</td>
<td>14</td>
</tr>
<tr>
<td>Certificate of Merger</td>
<td>2</td>
</tr>
<tr>
<td>Closing</td>
<td>1</td>
</tr>
<tr>
<td>Closing Date</td>
<td>2</td>
</tr>
<tr>
<td>Code</td>
<td>11</td>
</tr>
<tr>
<td>Company</td>
<td>1</td>
</tr>
<tr>
<td>Company Charter Documents</td>
<td>13</td>
</tr>
<tr>
<td>Company Contracts</td>
<td>26</td>
</tr>
<tr>
<td>Company Disclosure Schedules</td>
<td>12</td>
</tr>
<tr>
<td>Company Plans</td>
<td>20</td>
</tr>
<tr>
<td>Computer Systems</td>
<td>30</td>
</tr>
<tr>
<td>Contract</td>
<td>15</td>
</tr>
<tr>
<td>Convertible Securities</td>
<td>13</td>
</tr>
<tr>
<td>Copyrights</td>
<td>27</td>
</tr>
<tr>
<td>Deductible</td>
<td>56</td>
</tr>
<tr>
<td>DGCL</td>
<td>1</td>
</tr>
<tr>
<td>Effective Time</td>
<td>2</td>
</tr>
<tr>
<td>Engagement Letter</td>
<td>31</td>
</tr>
<tr>
<td>ERISA</td>
<td>20</td>
</tr>
<tr>
<td>Expiration Date</td>
<td>55</td>
</tr>
<tr>
<td>Financial Statements</td>
<td>16</td>
</tr>
<tr>
<td>Governmental Approval</td>
<td>15</td>
</tr>
<tr>
<td>Interim Period</td>
<td>49</td>
</tr>
<tr>
<td>Laws</td>
<td>18</td>
</tr>
<tr>
<td>Liens</td>
<td>13</td>
</tr>
<tr>
<td>Marks</td>
<td>27</td>
</tr>
<tr>
<td>Material Contract</td>
<td>25</td>
</tr>
<tr>
<td>Merger</td>
<td>1</td>
</tr>
<tr>
<td>Merger Sub</td>
<td>1</td>
</tr>
<tr>
<td>Multiemployer Plan</td>
<td>20</td>
</tr>
<tr>
<td>Parent</td>
<td>1</td>
</tr>
<tr>
<td>Parent Indemnifiable Losses</td>
<td>56</td>
</tr>
<tr>
<td>Parent Indemnified Parties</td>
<td>56</td>
</tr>
<tr>
<td>Patents</td>
<td>27</td>
</tr>
<tr>
<td>PBGC</td>
<td>21</td>
</tr>
<tr>
<td>Policies</td>
<td>30</td>
</tr>
<tr>
<td>Related Persons</td>
<td>36</td>
</tr>
<tr>
<td>Representatives</td>
<td>43</td>
</tr>
<tr>
<td>Restraints</td>
<td>50</td>
</tr>
<tr>
<td>Securities Act</td>
<td>13</td>
</tr>
<tr>
<td>Short Period</td>
<td>49</td>
</tr>
<tr>
<td>Subsidiary Documents</td>
<td>13</td>
</tr>
<tr>
<td>Surviving Company</td>
<td>1</td>
</tr>
<tr>
<td>Takeover Proposal</td>
<td>44</td>
</tr>
<tr>
<td>Tax Losses</td>
<td>57</td>
</tr>
<tr>
<td>Tax Returns</td>
<td>20</td>
</tr>
<tr>
<td>Tax Statement</td>
<td>48</td>
</tr>
<tr>
<td>Taxes</td>
<td>20</td>
</tr>
<tr>
<td>Trade Secrets</td>
<td>28</td>
</tr>
<tr>
<td>Unitholder Approval</td>
<td>14</td>
</tr>
<tr>
<td>Unitholder Representative Documents</td>
<td>64</td>
</tr>
<tr>
<td>Unitholder Representative Documents</td>
<td>64</td>
</tr>
<tr>
<td>Walk-Away Date</td>
<td>54</td>
</tr>
<tr>
<td>WARN</td>
<td>22</td>
</tr>
</tbody>
</table>
SECTION 9.13 Interpretation.

(a) When a reference is made in this Agreement to an Article, a Section, Exhibit or Schedule, such reference shall be to an Article of, a Section of, or an Exhibit or Schedule to, this Agreement unless otherwise indicated. The table of contents and headings contained in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement. Whenever the words “include”, “includes” or “including” are used in this Agreement, they shall be deemed to be followed by the words “without limitation”. The words “hereof”, “herein” and “hereunder” and words of similar import when used in this Agreement shall refer to this Agreement as a whole and not to any particular provision of this Agreement. All terms defined in this Agreement shall have the defined meanings when used in any certificate or other document made or delivered pursuant hereto unless otherwise defined therein. The definitions contained in this Agreement are applicable to the singular as well as the plural forms of such terms and to the masculine as well as to the feminine and neuter genders of such term. Except if otherwise explicitly provided, any agreement, instrument or statute defined or referred to herein or in any agreement or instrument that is referred to herein means such agreement, instrument or statute as from time to time amended, modified or supplemented, including (in the case of agreements or instruments) by waiver or consent and (in the case of statutes) by succession of comparable successor statutes and references to all attachments thereto and instruments incorporated therein. References to a Person are also to its permitted successors and assigns.

(b) The parties hereto have participated jointly in the negotiation and drafting of this Agreement and, in the event an ambiguity or question of intent or interpretation arises, this Agreement shall be construed as jointly drafted by the parties hereto and no presumption or burden of proof shall arise favoring or disfavoring any party by virtue of the authorship of any provision of this Agreement.

[signature page follows]
IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed and delivered as of the date first above written.

**PARENT:**

MAGELLAN HEALTH SERVICES, INC.

By: /s/ René Lerer  
Name:  
Title:  

**ACQUIRING CORP.:**

GREEN SPRING HEALTH SERVICES INC.

By: /s/ René Lerer  
Name:  
Title:  

**MERGER SUB:**

MAGELLAN SUB CO. II, INC.

By: /s/ René Lerer  
Name:  
Title:  

**THE COMPANY:**

ICORE HEALTHCARE LLC

By: /s/ Raju Mantena  
Name: Raju Mantena  
Title: President/CEO  

By: /s/ Raju Mantena  
Name: Raju Mantena  
Title:  

in his capacity as the representative for the Unitholders of ICORE HealthCare, LLC
This Limited Liability Company Agreement (this “Agreement”) of ICORE Healthcare, LLC (the “Company” or the “LLC”), dated as of __________, 2006, has been adopted pursuant to the Agreement and Plan of Merger, dated as of June 27, 2006 (the “Merger Agreement”), by and among Magellan Health Services, Inc., a Delaware corporation, Green Spring Health Services Inc., a Delaware corporation, Magellan Sub Co. II, Inc., a Delaware corporation, and the COMPANY, a Delaware limited liability company, upon the effective time (the “Effective Time”) of the merger (the “Merger”) of Magellan Sub Co. II, Inc. with and into the Company pursuant to such Agreement and Plan of Merger as provided in the Certificate of Merger of Icore Healthcare, LLC and Magellan Sub Co. II, Inc. filed with the office of the Secretary of State of the State of Delaware on _______ __, 2006.

WITNESSETH:

WHEREAS, Raju Mantena, as the initial member formed the Company as a limited liability company pursuant to and in accordance with the Delaware Limited Liability Company Act (6 Del.C. § 18-101, et seq.), as amended from time to time (the “Act”) by filing a Certificate of Formation with the Secretary of State of the State of Delaware on January 22, 2003 and entering into a Limited Liability Company Agreement, dated as of __________, 2003 (the “Initial Agreement”); and

WHEREAS, the Initial Agreement was amended and restated in its entirety, in part to add additional members listed on the signature pages hereto most recently as of March 31, 2004 (such agreement, the “March 2004 Amended and Restated Agreement”), which was in effect immediately before the Effective Time; and

WHEREAS, all of the members of the Company before the Effective time approved the Merger Agreement and the Merger; and

WHEREAS, as provided by the Merger Agreement, at the Effective Time (i) the Company was the surviving company of the Merger, (ii) the member interests in
the Company of all the members of the Company immediately before the Merger were cancelled in their entirety, (iii) Green Spring Health Services Inc. became the sole member of the Company and (iv) the March 2004 Amended and Restated Agreement was amended and restated in its entirety and replaced by this Amended and Restated Limited Liability Company Agreement;

NOW, THEREFORE, in consideration of the foregoing and of other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the following is adopted as the limited liability agreement of the COMPANY (the “Agreement”) as of the Effective Time:

ARTICLE I
ORGANIZATIONAL AND OTHER MATTERS

SECTION 1.01. Formation; Admission. The Company has previously been formed pursuant to the Act and is hereby continued under the Act. The rights and liabilities of the members of the Company shall be as provided for in the Act if not otherwise provided for in this Agreement as permitted by the Act. As of the Effective Time, Green Spring Health Services Inc. has been admitted to the Company as the sole member of the Company and any person who, prior to the Effective Time, was a member of the Company has ceased to be a member for all purposes and has ceased to have an further or continuing interest in or rights as a member of the Company.

SECTION 1.02. Name; Business. The name of the Company is ICORE Healthcare, LLC.

SECTION 1.03. Principal Office. The principal place of business and office of the Company shall be located at, and the Company’s business shall be conducted from, such place or places as may hereafter be determined by the Board of Managers of the LLC.

SECTION 1.04. Registered Office. The address of the registered office of the Company in the State of Delaware is c/o the Corporation Trust Company, Corporation Trust Center, 1209 Orange Street, Wilmington, DE 19801.

SECTION 1.05. Registered Agent. The name and address of the registered agent of the Company for service of process on the Company in the State of Delaware is c/o the Corporation Trust Company, Corporation Trust Center, 1209 Orange Street, Wilmington, DE 19801.

SECTION 1.06. Units. The entire membership interest in the Company shall be divided into 1,000 units, each of which shall be the same as each other. As of the Effective Time, Green Spring Health Services Inc. holds 1,000 Units and is the sole holder of units. The holder of a Unit is hereinafter referred to as a “Member. References herein to “Members” shall refer to the sole member at any time when there is only one member.
SECTION 1.07. **Term.** The term of the Company commenced on the date of filing of the Certificate of Formation of the Company on January 22, 2003 in accordance with the Act and shall continue until dissolution of the Company in accordance with this Agreement.

SECTION 1.08. **Fiscal Year.** The fiscal year of the Company for financial reporting and tax purposes shall be the calendar year, unless otherwise provided by an amendment to this Agreement.

SECTION 1.09. **Limited Liability.** Except as otherwise provided by the Act, the debts, obligations and liabilities of the Company, whether arising in contract, tort or otherwise, shall be the debts, obligations and liabilities solely of the Company, and no Member nor any manager, officer, employee or agent of the Company (including a person having more than one such capacity) shall be obligated personally for any of such debts, obligations or liabilities solely by reason of acting in such capacity.

SECTION 1.10. **Disregarded Entity.** The LLC shall be treated as a disregarded entity for Federal income tax purposes.

**ARTICLE II**

**PURPOSE AND POWERS**

SECTION 2.01. **Purpose of the Company.** The Company may carry on any lawful business, purpose or activity permitted by the Act.

SECTION 2.02. **Powers of the LLC.** The Company shall have the power to do any and all acts reasonably necessary, appropriate, proper, advisable, incidental or convenient to or for the furtherance of the purpose and business described herein and for the protection and benefit of the Company.

**ARTICLE III**

**CAPITAL CONTRIBUTIONS**

**Capital Contributions.** At the Effective Time, Green Spring Health Services Inc. succeeded to the aggregate capital contributions of the members immediately before the Effective Time, as indicated on Exhibit A hereto, and such aggregate capital contribution shall be considered its capital contribution to the Company. No Member is required to make any additional capital contributions to the Company.
ARTICLE IV
DISTRIBUTIONS

Distribution of Proceeds. Distributions shall be made to the Member at the times and in the aggregate amounts determined by the Board of Managers.

ARTICLE V
MEMBER ACTION

SECTION 5.01. Action Without a Meeting. Any action that may be taken by the members of a limited liability company under the Act at a meeting may be taken without a meeting if a consent in writing setting forth the action to be taken is signed by the Members having a sufficient interest in the Company for the taking of such action, as determined in accordance with the Act and this Agreement.

SECTION 5.02. Procedures. A member shall be entitled to cast votes: (a) at a meeting, either in person or by a signed writing directing the manner in which the vote is to be cast, which writing must be received by the Secretary or the Assistant Secretary of the LLC at or prior to the commencement of the meeting; or (b) without a meeting, by a signed writing directing the manner in which the vote is to be cast, which writing must be received by the Secretary or an Assistant Secretary of the LLC. Other procedures of any member meeting shall be as determined by the Member.

SECTION 5.03. Management. The Member, in its capacity as a Member, shall not participate in the management or control of the business of, and shall not have any rights or powers with respect to the management of, the LLC except those expressly granted to it by the terms of this Agreement or those conferred on it by law.

ARTICLE VI
MANAGEMENT OF THE LLC

SECTION 6.01. Board of Managers. In accordance with Section 18-402 of the Act, management of the LLC shall be vested in the board of managers of the Company (the “Board of Managers”). The Board of Managers shall consist of not less than three nor more than nine individual (the “Managers”), as determined and to be selected by vote of the Member or Members. Unless otherwise provided by vote of the Members, the number of members of the Board of Managers will be three. As of the Effective Time, the initial Managers shall be ______________, _______________ and ________________. Managers do not have to hold Units in the Company as Members of the Company in order to serve as a Manager. The Board of Managers shall have the power to do any and all acts necessary, convenient or incidental to or for the furtherance of the purposes described herein, including all powers, statutory or otherwise, possessed by managers of a limited liability company under the laws of the State of Delaware and including all things necessary to carry out the terms and provisions of this Agreement. The Board of Managers has the authority to bind the Company.
The Board of Managers shall hold regular meetings not less frequently than once every year at a time and place fixed by the Board of Managers and otherwise shall meet when called by any Manager or the President or Secretary of the Company upon reasonably notice given to all Managers. A quorum for action at a meeting of the Managers shall be a majority of the members of the entire Board of Managers. The vote of a majority of the Managers present at a meeting of the Board of Managers at which a quorum is present shall be the act of the Board of Managers. The Board of Managers may also act by unanimous written consent of the Managers then in office stating the action to be taken, effective when signed by all the Managers then in office unless another effective date is stated therein.

Managers may withdraw at any time. Managers may be removed at any time for any reason or no reason upon the written direction of the Members. If any Manager is removed or shall have resigned or become unable to serve, then the remaining Managers shall have the power to designate a person to fill such vacancy; vacancies may also be filled by action of the Members.

SECTION 6.02. Officers. The Board of Managers shall designate in writing from time to time the following officers of the Company: President, Secretary and Treasurer and may, as it deems advisable, appoint other officers of the Company and assign in writing titles to any such person (collectively the “Officers”). Each Officer shall be appointed to serve until his or her respective successor is appointed and qualified. The same person may hold two or more offices. Each Officer will have the authority to execute agreements on behalf of the Company with respect to those documents which are commonly signed by such officers of a business corporation formed under the Delaware General Corporation Law.

Unless the Board of Managers decides otherwise, if the title assigned to an Officer is one commonly used for officers of a business corporation formed under the Delaware General Corporation Law, the assignment of such title shall constitute the delegation to such person of the authorities and duties that are normally associated with that office.

Any Officer designated by the Board of Managers may be removed, either for or without cause, at any time by the Board of Managers. Any Officer who is not a member of the Board of Managers may be removed from office by the President.

Any Officer or agent may resign at any time by giving written notice to the Board of Managers. Any such resignation shall take effect at the date of the receipt of such notice or at any later time specified therein and, unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective.

A vacancy in any office because of death, resignation, removal, disqualification, or any other cause, shall be filled by any such person as may be appointed by the Board of Managers.
SECTION 6.03. Exculpation and Indemnification. None of the Members, Managers or Officers (each an “Indemnified Party”) shall be liable to the LLC for any loss, damage or claim (a “Loss”) (or any expenses or costs associated therewith (“Costs”)) incurred by reason of any act or omission performed or omitted by such Indemnified Party in good faith on behalf of the LLC and in a manner reasonably believed to be within the scope of the authority conferred on such Indemnified Party by this Agreement, except that an Indemnified Party shall be liable for any such Loss and Costs, incurred by reason of such Indemnified Party’s gross negligence or willful misconduct. To the full extent permitted by applicable law, an Indemnified Party shall be entitled to indemnification from the Company for any Loss or Costs incurred by such Indemnified Party by reason of any act or omission performed or omitted by such Indemnified Party in good faith on behalf of the LLC and in a manner reasonably believed to be within the scope of the authority conferred on such Indemnified Party by this Agreement, except that no Indemnified Party shall be entitled to be indemnified in respect of any Loss or Costs incurred by such Indemnified Party by reason of such Indemnified Party’s gross negligence or willful misconduct with respect to such acts or omissions; provided, however, that any indemnity under this Section 6.03 shall be provided out of and to the extent of LLC assets only, and no Member, Manager or Officer shall have personal liability on account thereof. The Company shall advance Costs incurred by or on behalf of an Indemnified Party in connection with any Loss within twenty (20) days after receipt by the Company from the Indemnified Party of a statement requesting such advances from time to time; provided such statement provides reasonable documentary evidence of such Costs and provides a written undertaking by the Indemnified Party to repay any and all advanced Costs in the event such Indemnified Party is ultimately determined to not be entitled to indemnification by the Company.

ARTICLE VI
TRANSFER OF MEMBERSHIP INTERESTS

Transfer Restrictions. Units of member interests in the Company are not transferable except with the approval of a majority in interest of the Members.

ARTICLE VII
DISSOLUTION AND LIQUIDATION

SECTION 7.01. Dissolution. The Company shall dissolve, and its affairs shall be wound up, upon the first to occur of the following: (i) the written consent of a majority of the Board of Managers and the consent of the Members, (ii) the sale of all of the assets of the Company; and (iii) the entry of a decree of judicial dissolution under Section 18-802 of the Act.

SECTION 7.02. Effect of Dissolution. Upon dissolution, the LLC shall cease carrying on its business but shall not terminate until the winding up of the affairs of the LLC is completed, the assets of the LLC shall have been distributed as provided.
below and a Certificate of Cancellation of the LLC under the Act has been filed with the Secretary of State of the State of Delaware.

SECTION 7.03. Liquidation Upon Dissolution. Upon the dissolution of the LLC, authority to effectuate the liquidation of the assets of the LLC shall be vested in the Board of Managers unless otherwise determined by act of the Members, which shall have full power and authority to sell, assign and encumber any and all of the LLC’s assets and to wind up and liquidate the affairs of the LLC in an orderly and business-like manner. The proceeds of liquidation of the assets of the LLC distributable upon a dissolution and winding up of the LLC shall be applied in the following order of priority:

(i) first, to the creditors of the LLC, including the Member, in the order of priority provided by law, in satisfaction of all liabilities and obligations of the LLC (of any nature whatsoever, including, without limitation, fixed or contingent, matured or unmatured, legal or equitable, secured or unsecured), whether by payment or the making of reasonable provision for payment thereof; and

(ii) thereafter, to the Members.

SECTION 7.04. Winding Up and Articles of Dissolution. The winding up of the LLC shall be completed when all of its debts, liabilities, and obligations have been paid and discharged or reasonably adequate provision therefor has been made, and all of the remaining property and assets of the LLC have been distributed to the Members. Upon the completion of the winding up of the LLC, a Certificate of Cancellation of the LLC shall be filed with the Secretary of State of the State of Delaware.

ARTICLE VIII
AMENDMENT

Amendment Procedures. This Agreement may be amended or modified only by a written instrument executed by the Members. In addition, the terms or conditions hereof may be waived only by a written instrument executed by the Members.

[Remainder of page intentionally left blank.]
IN WITNESS WHEREOF, this Limited Liability Company Agreement has been executed by the undersigned as of the date first written above.

MEMBER:

Green Spring Health Services Inc.

By:

Name:
Title:

8
<table>
<thead>
<tr>
<th>Name/Address</th>
<th>Aggregate Capital Contribution</th>
<th>Units</th>
</tr>
</thead>
<tbody>
<tr>
<td>Green Spring Health Services Inc. 55 Nod Road Avon, Connecticut 06601</td>
<td>$77,000</td>
<td>1,000</td>
</tr>
</tbody>
</table>
The Company’s “Adjusted EBITDA” for any period referred to in paragraphs (i), (ii) and (iii) of Section 2.1(c) shall mean the Company’s earnings before interest expense, income taxes, depreciation and amortization, as customarily determined in accordance with good business practice except as set forth herein, as adjusted as hereinafter provided. In particular, Adjusted EBITDA shall reflect the Company’s gross revenues, determined in accordance with GAAP, for such period less the sum of (1) the Company’s cost of goods sold, determined in accordance with GAAP, and (2) general and administrative expenses which shall include all direct expenses of the Company’s operations as well as indirect expenses related to the support of the Company’s operations but shall not include after the Closing any allocation of overhead costs of the Parent (as distinguished from administrative costs of the Company’s operations administered by the Parent), even though otherwise allocable to the Company in accordance with Parent’s customary accounting practice, determined in accordance with GAAP, and excluding any compensation charges relating to the payment of any portion of the Merger Consideration, and (3) depreciation and amortization in respect of all capital expenditures incurred after the Closing by the Company or on behalf of the Company’s operations, determined in accordance with GAAP, but not including amortization or impairment of goodwill and/or any other intangible assets created by the Merger, and without any charge to provide for the Company’s federal, state or local incomes tax liability on its taxable income, provided that (A) the Company’s revenues and cost of goods sold and general and administrative expenses shall be determined on a basis consistent with that used in the preparation of the Company’s audited financial statements audited by Mayer Hoffman McCann, P.C. for the year ended December 31, 2005 referred to in Section 3.5, (B) the Company’s depreciation and amortization with respect to capital expenditures incurred after the Closing shall be determined on a basis consistent with the basis for the determination of depreciation, amortization and capital expenditures by Parent customarily used in the preparation of its financial reports. Except as expressly provided in this Exhibit 2.1(d), for purposes of this Agreement, the separate components of the Company’s Adjusted EBITDA shall be calculated on a basis consistent with the practices used in the preparation of Parent’s financial statements as filed with the SEC. Parent shall deliver to the Unitholder Representative by the First Earn-out Distribution Date or the Second Earn-out Distribution Date, as the case may be, a certificate, signed by its Chief Financial Officer and Chief Accounting Officer or Controller certifying to the calculation of the Company’s Adjusted EBITDA for the periods referred to in paragraph (i), (ii) or (iii) of Section 2.1(c), as pertinent.

If the Unitholder Representative shall object in writing to any calculation of Adjusted EBITDA for any period referenced in paragraph (i), (ii) and (iii) of Section 2.1(c) within thirty (30) days after receiving notice of such determination, then the Unitholder Representative and Parent shall attempt in good faith to resolve their disagreement with respect to the calculation of Adjusted EBITDA. If no such agreement can be reached after good faith negotiation within thirty (30) days after delivery of the
Unitholder’s written obligation, Parent and the Unitholder Representative shall select a mutually acceptable independent accountant (the “Independent Accountant”), who shall determine the Company’s Adjusted EBITDA for their relevant period, and whose determination shall be final and binding on the parties for purposes of this Agreement. The Independent Accountant’s fees and expenses shall be borne as follows: if the Independent Accountant determines that the Company’s Adjusted EBITDA is greater than the amount initially calculated by Parent, then Parent shall pay the fees and expenses; if the Independent Accountant determines that the Company’s Adjusted EBITDA is less than or equal to the amount initially calculated by Parent, then the Unitholders shall pay the fees and expenses.
Individuals:

Raju Mantena
George Petrovas
Kjel Johnson
Andrew Gellman
Kerry Bradley

Employment Agreements:

1. Employment Agreement, dated June 27, 2006, by and between Raju Mantena and Magellan Health Services, Inc.
2. Employment Agreement, dated June 27, 2006, by and between George Petrovas and Magellan Health Services, Inc.
3. Employment Agreement, dated June 27, 2006, by and between Kjel Johnson and Magellan Health Services, Inc.
5. Employment Agreement, dated June 27, 2006, by and between Kerry Bradley and Magellan Health Services, Inc.
Officer’s Certificate

The undersigned, being the duly elected and incumbent chief executive [ / chief financial] officer of ICORE Healthcare LLC, a Delaware limited liability company (the “Company”), does hereby certify to Magellan Health Services, Inc. (“Parent”), as provided by Section 6.2(a) of the Agreement and Plan of Merger dated as of June __, 2006, by and among the Company, Green Spring Health Services Inc. and Magellan Sub Co. II, Inc. that:

1. Based on my knowledge, the audited financial statements of the Company for the year ended December 31, 2005, previously delivered to Parent, fairly present in all material respects the financial condition, results of operations and cash flows of the Company as of, and for, the periods presented in such report.

2. The Company’s chief financial [ / executive] officer and I are responsible for establishing and maintaining the Company’s internal control over financial reporting (as defined in Rules 13a-15(f) under the Securities Exchange Act of 1934, as amended) for the Company and have designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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.

3. I have disclosed to Parent in writing any change in the Company’s internal control over financial reporting known to me that occurred during the Company’s most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting.

4. I have disclosed to Parent in writing (a) all significant deficiencies and material weaknesses in the design or operation of the Company internal control over financial reporting known to me which are reasonably likely to adversely affect the Company’s ability to record, process, summarize and report financial information; and (b) any fraud, whether or not material, known to me that involves management or other employees who have a significant role in the Company’s internal control over financial reporting.

Date:

________________________
Name:

Title: [chief executive [ / financial] officer]
1. Purpose

2. Administration
   (a) Committee
   (b) Authority
   (c) Delegation and Advisers
   (d) Limitation of Liability and Indemnification

3. Participants

4. Type of Awards

5. Common Stock Available Under the Plan
   (a) Basic Limitations
   (b) Additional Shares
   (c) Business Acquisition Grants

6. Stock Options
   (a) Generally
   (b) Exercise Price
   (c) Payment of Exercise Price
   (d) Exercise Period
   (e) Limitations on Incentive Stock Options
   (f) Additional Limitations on Incentive Stock Options for Ten Percent Shareholders

7. Stock Appreciation Rights
   (a) Generally
   (b) Exercise Period

8. Restricted Stock Awards
   (a) Generally
   (b) Payment of the Purchase Price
   (c) Additional Terms
   (d) Rights as a Shareholder
9. Stock Units
   (a) Generally
   (b) Settlement of Stock Units
   (c) Definitions

10. Performance-Based Awards
    (a) Generally
    (b) Business Criteria
    (c) Establishment of Performance Goals
    (d) Certification of Performance
    (e) Modification of Performance-Based Awards

11. Foreign Laws

12. Certain Terminations of Employment; Forfeitures
    (a) Forfeiture of Unsettled Awards
    (b) Effect on Settled Awards
    (c) Timing
    (d) Determination from the Committee
    (e) Condition Precedent
    (f) Enforceability


14. Nontransferability

15. Other Provisions

16. Fair Market Value

17. Withholding

18. Employment Rights

19. Tax Compliance
    (a) Certain Limitations on Awards to Ensure Compliance with Section 409A
    (b) Certain Terms Relating to Code Section 409A
    (c) Unfunded Plan

20. No Fractional Shares

21. Duration, Amendment and Termination

22. Governing Law

23. Effective Date
## Index of Defined Terms

<table>
<thead>
<tr>
<th>Term</th>
<th>Section Where Defined or First Used</th>
</tr>
</thead>
<tbody>
<tr>
<td>Awards</td>
<td>4</td>
</tr>
<tr>
<td>Code</td>
<td>2(a)</td>
</tr>
<tr>
<td>Committee</td>
<td>2(a)</td>
</tr>
<tr>
<td>Common Stock</td>
<td>5(a)</td>
</tr>
<tr>
<td>Company</td>
<td>1</td>
</tr>
<tr>
<td>Dividend Equivalent Right.</td>
<td>9(c)</td>
</tr>
<tr>
<td>Effective Date</td>
<td>23</td>
</tr>
<tr>
<td>Exchange Act</td>
<td>2(a)</td>
</tr>
<tr>
<td>Fair Market Value</td>
<td>16</td>
</tr>
<tr>
<td>Incentive Stock Option</td>
<td>6(a)</td>
</tr>
<tr>
<td>Injurious Conduct</td>
<td>12(a)</td>
</tr>
<tr>
<td>Non-Employee Director</td>
<td>2(a)</td>
</tr>
<tr>
<td>Nonqualified Stock Option.</td>
<td>6(a)</td>
</tr>
<tr>
<td>Parent Corporation</td>
<td>6(c)</td>
</tr>
<tr>
<td>Performance-Based Awards</td>
<td>10(a)</td>
</tr>
<tr>
<td>Plan</td>
<td>1</td>
</tr>
<tr>
<td>Restricted Stock Award</td>
<td>8</td>
</tr>
<tr>
<td>Stock Appreciation Rights</td>
<td>7</td>
</tr>
<tr>
<td>Stock Options</td>
<td>6</td>
</tr>
<tr>
<td>Stock Unit</td>
<td>9(c)</td>
</tr>
<tr>
<td>Subsidiary Corporation</td>
<td>6(c)</td>
</tr>
</tbody>
</table>
1. Purpose. The Magellan Health Services, Inc. 2006 Management Incentive Plan (the “Plan”) is intended to provide incentives which will attract, retain and motivate highly competent persons as officers and employees of Magellan Health Services, Inc., a Delaware corporation (the “Company”), and its subsidiaries and affiliates, by providing them with appropriate incentives and rewards to encourage them to enter into and continue in the employ of the Company, to acquire a proprietary interest in the long-term success of the Company and to reward the performance of individuals in fulfilling their personal responsibilities for achievement of the Company’s objectives.

2. Administration.

(a) Committee. The Plan will be administered by a committee (the “Committee”) appointed by the Board of Directors of the Company from among its members and shall be comprised, unless otherwise determined by the Company’s Board of Directors, solely of not less than two (2) members who shall be (i) “Non-Employee Directors” within the meaning of Rule 16b-3(b)(3) (or any successor rule) promulgated under the Securities Exchange Act of 1934, as amended (the “Exchange Act”) and (ii) “outside directors” within the meaning of Treasury Regulation Section 1.162-27(e)(3) under Section 162(m) of the Internal Revenue Code of 1986, as amended (the “Code”). The Board of Directors may perform any function of the Committee hereunder, in which case references to the Committee shall be deemed to include the Board. The foregoing notwithstanding, no action or decision of the Committee shall be void or deemed not duly authorized solely because a member of the Committee did not meet a qualification requirement set forth in this Section 2(a).

(b) Authority. The Committee is authorized, subject to the provisions of the Plan, to make and administer grants under the Plan (including to determine the terms and conditions of Awards granted and to waive conditions initially established for grants, including to accelerate vesting and to extend the exercisability of grants, except as specifically restricted by this Plan) and to establish such rules and regulations as it deems necessary for the proper administration of the Plan, including to make such determinations and interpretations and to take such action in connection with the Plan and any Awards granted hereunder as it deems necessary or advisable to carry out its purposes. All determinations and interpretations made by the Committee shall be binding and conclusive on all participants and their legal representatives.

(c) Delegation and Advisers. The Committee may delegate to one or more of its members (including to a designated subcommittee), to management of the Company, to counsel for or advisors or consultants to the Committee or to one or more other agents appointed by the Committee, such administrative duties as the Committee may deem advisable; provided, such delegation does not adversely effect the exemption provided by Rule 16b-3 of the Exchange Act, prevent an Award from qualifying as a Performance-Based Award, if so intended, complying with Section 157 of the Delaware General Corporation Law and otherwise complying with applicable law. The Committee, or any person to whom it has delegated duties as aforesaid, may employ one or more persons to render advice with respect to any responsibility the Committee or such person may have under the Plan. The Committee may employ such legal or other counsel, consultants and agents as it may deem desirable for the administration of the Plan and may rely upon any opinion or computation received from any such counsel, consultant or agent. Expenses incurred by the Committee in the engagement of such counsel, consultant or agent, shall be paid by the Company, or the subsidiary or affiliate whose employees have benefited from the Plan, as determined by the Committee.
3. Participants. Participants will consist of such officers and employees of the Company and its subsidiaries and affiliates as the Committee in its sole discretion determines to be responsible for the success and future growth and profitability of the Company and whom the Committee may designate from time to time to receive Awards under the Plan. Designation of a participant in any year shall not require the Committee to designate such person to receive an Award in any other year or, once designated, to receive the same type or amount of Award as granted to the participant in any other year. The Committee shall consider such factors as it deems pertinent in selecting participants and in determining the type and amount of their respective Awards.

4. Type of Awards. Awards under the Plan may be granted in any one or a combination of (a) Stock Options, (b) Stock Appreciation Rights, (c) Restricted Stock Awards and (d) Stock Units (each as described below, and collectively, the “Awards”). Any Award may, as determined by the Committee in its discretion, constitute Performance-Based Awards, as described in Section 10 hereof. Awards granted under the Plan shall be evidenced by an agreement (which need not be identical with respect to each grant or grantee) that may provide additional terms and conditions associated with such Awards, as determined by the Committee in its sole discretion, provided, however, that in the event of any conflict between the provisions of the Plan and any such agreement, the provisions of the Plan shall prevail. Nothing contained herein shall prevent the Company from making cash bonus payments or providing other Awards pursuant to any employment agreement, bonus plan or arrangement or other compensation or benefit plan or program.


(a) Basic Limitations. The aggregate number of shares of capital stock of the Company that may be delivered in connection with Awards granted under this Plan shall be 2,750,000 shares of Ordinary Common Stock (the “Common Stock”), which may be authorized and unissued shares or treasury shares or may be purchased on the open market or by private purchase, provided that the maximum number of shares of Common Stock that may be delivered in connection with Restricted Stock Awards or Stock Units shall be 300,000. The number of shares of Common Stock that may be delivered under the Plan shall be subject to adjustments in accordance with Section 13 hereof and Sections 5(b) and 5(c) hereof. The maximum number of shares of Common Stock with respect to which Awards may be granted to or measured with respect to any individual participant under the Plan in any one calendar year shall not exceed 2,000,000 (subject to adjustments made in accordance with Section 13 hereof.

(b) Additional Shares. Any shares of Common Stock which are: (i) underlying a Stock Option or Stock Appreciation Right which is cancelled or terminated without having been exercised, including due to expiration or forfeiture, (ii) subject to Restricted Stock Awards or Stock Units which are cancelled, terminated or forfeited, (iii) not delivered to a participant because all or a portion of a Restricted Stock
Award or Award of Stock Units is settled in cash, or (iv) withheld in connection with a Restricted Stock Award or Stock Units to satisfy tax withholding obligations, shall in each case again be available for Awards under the Plan (with shares subject to such Restricted Stock Awards or Stock Units again available for those types of Awards). Any shares of Common Stock covered by a Stock Option or Stock Appreciation Rights shall be deemed to be delivered upon exercise with respect to such underlying shares even if the net number of shares delivered to the participant is less than the number of shares underlying the Award (as would occur, for example, upon a net exercise of options, upon a settlement of Stock Appreciation Rights in cash or for a net number of shares, upon a stock-for-stock exercise of Stock Options, or upon share withholding to satisfy tax obligations upon exercise of Stock Options or Stock Appreciation Rights). The preceding sentences of this Section shall apply only for purposes of determining the aggregate number of shares of Common Stock subject to Awards delivered in connection with Awards, or generally available for Awards, but shall not apply for purposes of determining the maximum number of shares of Common Stock with respect to which Awards may be granted to any individual participant in any calendar year under the Plan.

(c) Business Acquisition Grants. In connection with the acquisition of any business by the Company or any of its subsidiaries or affiliates, any then outstanding options or other similar rights or other equity awards pertaining to such business may be assumed or replaced by Awards under the Plan upon such terms and conditions as the Committee determines in its sole discretion and, to the extent any shares of Common Stock are to be delivered as Awards under the Plan in replacement for any such grants, awards, options or rights of another business, such shares shall be in addition to those available for the grant of Awards as provided by Sections 5(a) and 5(b).


(a) Generally. Stock Options will consist of awards from the Company that will enable the holder to purchase a number of shares of Common Stock, at set terms. Stock Options may be “incentive stock options” (“Incentive Stock Options”), within the meaning of Section 422 of the Code, or Stock Options which do not constitute Incentive Stock Options (“Nonqualified Stock Options”). The Committee will have the authority to grant to any participant one or more Incentive Stock Options, Nonqualified Stock Options, or both types of Stock Options (in each case with or without Stock Appreciation Rights). Each Stock Option shall be subject to such terms and conditions, including vesting (which may be accelerated, including upon a change of control of the Company), consistent with the Plan as the Committee may impose or determine from time to time, subject to the following limitations.

(b) Exercise Price. Each Nonqualified Stock Option granted hereunder shall have a per-share exercise price as the Committee may determine on the date of grant, but not less than 100% of the Fair Market Value of a share at the date of grant.

(c) Payment of Exercise Price. The option exercise price may be paid in cash or, in the discretion of the Committee, by the delivery of shares of Common Stock of the Company then owned by the participant, or, in the case of Nonqualified Stock Options, by directing the Company to withhold shares otherwise deliverable upon exercise to satisfy the exercise price. In the discretion of the Committee, payment may also be made by delivering a properly executed exercise notice to the Company together with a copy of irrevocable instructions to a broker to deliver promptly to the Company the amount of sale or loan proceeds to pay the exercise price as long as such transaction does not constitute an impermissible loan to an executive officer under Section 13(k) of the Exchange Act (Section 402 of the Sarbanes-Oxley Act of 2002). To facilitate the foregoing, the Company may enter into agreements for coordinated procedures with one or more brokerage firms. The Committee may prescribe any other method of paying the exercise price that it determines to be consistent with applicable law and the purpose of the Plan, including, without limitation, in lieu of the exercise of a Stock Option by delivery of shares of Common Stock of the Company then owned by a participant, providing the Company with a notarized statement attesting to the number of...
shares owned, where upon verification by the Company, the Company would issue to the participant only the number of incremental shares to which the participant is entitled upon exercise of the Stock Option.

(d) Exercise Period. Stock Options granted under the Plan shall be exercisable at such time or times and subject to such terms and conditions, including vesting, as shall be determined by the Committee; provided, however, that no Stock Option shall be exercisable later than ten (10) years after the date it is granted. All Stock Options shall terminate at such earlier times and upon such conditions or circumstances as the Committee shall in its discretion set forth in such option agreement on the date of grant.

(e) Limitations on Incentive Stock Options. Incentive Stock Options may be granted only to participants who are employees of the Company or of a “Parent Corporation” or “Subsidiary Corporation” (as defined in Sections 424(e) and (f) of the Code, respectively) on the date of grant. The aggregate Fair Market Value (determined as of the time the Stock Option is granted) of the Common Stock with respect to which Incentive Stock Options are exercisable for the first time by a participant during any calendar year (under all option plans of the Company and of any Parent Corporation or Subsidiary Corporation) shall not exceed one hundred thousand dollars ($100,000); provided, however, that if such $100,000 limit is exceeded, the excess Incentive Stock Options shall be treated as Nonqualified Stock Options. For purposes of the preceding sentence, Incentive Stock Options will be taken into account in the order in which they are granted. The per-share exercise price of an Incentive Stock Option shall not be less than one hundred percent (100%) of the Fair Market Value of the Common Stock on the date of grant, and no Incentive Stock Option may be exercised later than ten (10) years after the date it is granted.

(f) Additional Limitations on Incentive Stock Options for Ten Percent Shareholders. Incentive Stock Options may not be granted to any participant who, at the time of grant, owns stock possessing (after the application of the attribution rules of Section 424(d) of the Code) more than ten percent (10%) of the total combined voting power of all classes of stock of the Company or any Parent Corporation or Subsidiary Corporation, unless the exercise price of the option is fixed at not less than one hundred ten percent (110%) of the Fair Market Value of the Common Stock on the date of grant and the exercise of such option is prohibited by its terms after the expiration of five (5) years from the date of grant of such option.

7. Stock Appreciation Rights.

(a) Generally. The Committee may, in its discretion, grant Stock Appreciation Rights, including a concurrent grant of Stock Appreciation Rights in tandem with any Stock Option grant. A Stock Appreciation Right means a right to receive a payment in cash, Common Stock or a combination thereof, as determined by the Committee, in an amount equal to the excess of (i) the Fair Market Value, or other specified valuation (which may not exceed Fair Market Value), of a specified number of shares of Common Stock on the date the right is exercised over (ii) the Fair Market Value of such shares of Common Stock on the date the right is granted, or other specified amount (which may not be less than Fair Market Value), all as determined by the Committee; provided, however, that if a Stock Appreciation Right is granted in tandem with or in substitution for a Stock Option, the designated Fair Market Value in the award agreement shall reflect the Fair Market Value on the date such Stock Option was granted. Each Stock Appreciation Right shall be subject to such terms and conditions including vesting (which may be accelerated, including upon a change of control of the Company, subject to Section 19(a)), as the Committee shall impose or determine from time to time; provided, however, that if a Stock Appreciation Right is granted in connection with a Stock Option, the Stock Appreciation Right shall become exercisable and shall expire according to the same vesting and expiration rules as the corresponding Stock Option, unless otherwise determined by the Committee.

(b) Exercise Period. Stock Appreciation Rights granted under the Plan shall be exercisable at such time or times and subject to such terms and conditions including vesting (which may be accelerated, including upon a change of control of the Company, subject to Section 19(a)), as shall be determined by the Committee; provided, however, that no Stock Appreciation Rights shall be exercisable later than ten
(10) years after the date it is granted; and provided further, that the time of exercise of any SAR intended to be a 409A Award shall conform to applicable requirements of Code Section 409A. All Stock Appreciation Rights shall terminate at such earlier times and upon such conditions or circumstances as the Committee shall in its discretion set forth in such right at the date of grant.

8. Restricted Stock Awards.

(a) Generally. The Committee may, in its discretion, grant Restricted Stock Awards consisting of Common Stock issued or transferred to participants with or without cash or other payment therefor in whole or in part. Each participant granted a Restricted Stock Award shall execute and deliver to the Company an agreement with respect to the Restricted Stock setting forth the restrictions applicable to such Restricted Stock.

(b) Payment of the Purchase Price. If the Restricted Stock Award requires payment therefor, the purchase price of any shares of Common Stock subject to a Restricted Stock Award may be paid in any manner authorized by the Committee, which may include any manner authorized under the Plan for the payment of the exercise price of a Stock Option. Restricted Stock Awards may also be made solely in consideration of services rendered to the Company or its subsidiaries or affiliates. This may include treating services between the grant date and the date of issuance as payment of lawful consideration equal to the par value of the Restricted Stock Award.

(c) Additional Terms. Restricted Stock Awards may be subject to such terms and conditions including vesting (which may be accelerated, including upon a change of control of the Company), as the Committee determines appropriate, including, without limitation, (i) restrictions on the sale or other disposition of such shares, and (ii) the right of the Company to reacquire such shares for no consideration upon termination of the participant’s employment within specified periods, the participant’s competition with the Company, or the participant’s breach of other obligations to the Company. Restricted Stock Awards not subject to a vesting requirements are authorized hereunder. Restricted Stock Awards may constitute Performance-Based Awards, as described in Section 10 hereof. The Committee may require the participant to deliver a duly signed stock power, endorsed in blank, relating to the Common Stock covered by such an Award. The Committee may also require that the stock certificates evidencing such shares be held in custody or bear restrictive legends until the restrictions thereon shall have lapsed.

(d) Rights as a Shareholder. The participant shall have, with respect to the shares of Common Stock subject to a Restricted Stock Award, all of the rights of a holder of shares of Common Stock of the Company, including the right to vote the shares, except as may be otherwise provided in a Restricted Stock Award agreement as determined by the Committee. At the discretion of the Committee, cash dividends and stock dividends with respect to the Restricted Stock may be either currently paid to the participant or withheld by the Company for the participant’s account, and interest may be credited on the amount of cash dividends withheld at a rate and subject to such terms (which may be accelerated, including upon a change of control of the Company) as determined by the Committee. The cash dividends or stock dividends so withheld by the Committee and attributable to any particular share of Restricted Stock (and earnings thereon, if applicable) shall be distributed to the participant upon the release of restrictions on such shares and, if such share is forfeited, the participant shall have no right to such cash dividends or stock dividends.

9. Stock Units.

(a) Generally. The Committee may, in its discretion, grant Stock Units (as defined in subsection (c) below) to participants hereunder. Stock Units may be subject to such terms and conditions including vesting (which may be accelerated, including upon a change of control of the Company, subject to Section 19(a)), as the Committee determines appropriate. Stock Units may constitute Performance-Based Awards, as described in Section 10 hereof. A Stock Unit granted by the Committee shall provide payment in shares of Common Stock at such time as the award agreement shall specify. Stock Units may be 409A.
Awards or Non-409A Awards, based upon their terms; the Committee may include elective deferral features for Stock Units in its discretion. Shares of Common Stock issued pursuant to this Section 9 may be issued with or without other payments therefor as may be required by applicable law or such other consideration as may be determined by the Committee. The Committee shall determine whether a participant granted a Stock Unit shall be entitled to a Dividend Equivalent Right (as defined in subsection (c) below).

(b) **Settlement of Stock Units.** Shares of Common Stock representing the Stock Units shall be distributed to the participant unless the Committee provides for the payment of the Stock Units in cash equal to the value of the shares of Common Stock which would otherwise be distributed to the participant or partly in cash and partly in shares of Common Stock.

(c) **Definitions.** A “Stock Unit” means a notional account representing a participant’s conditional right to receive at a future date one (1) share of Common Stock. A “Dividend Equivalent Right” means the right to receive the amount of any dividend paid on the share of Common Stock underlying a Stock Unit, which shall be payable in cash or in the form of additional Stock Units, and subject to a risk of forfeiture and other terms as specified by the Committee.

10. **Performance-Based Awards.**

(a) **Generally.** Any Awards granted under the Plan may be granted in a manner such that the Awards qualify for the performance-based compensation exemption of Section 162(m) of the Code (“Performance-Based Awards”). As determined by the Committee in its sole discretion, either the granting or vesting of such Performance-Based Awards shall be based on achievement of performance objectives that are based on one or more of the business criteria described below that apply to the individual participant, one or more business units or the Company as a whole.

(b) **Business Criteria.** The business criteria shall be as follows, individually or in combination: (i) net earnings; (ii) earnings per share; (iii) revenues; (iv) sales; (v) operating income; (vi) earnings before interest and taxes (EBIT); (vii) earnings before interest, taxes, depreciation and amortization (EBITDA); (viii) segment profit, as defined in the company’s financial statements; (ix) working capital targets; (x) return on equity; (xi) return on capital or return on assets; (xii) expenses or expense ratios; (xiii) cash flow, free cash flow, cash flow return on investment, net cash provided by operations, or economic profit created; (xiv) market price per share; (xv) total return to shareholders, and (xvi) specific strategic or operational business criteria, including market penetration, geographic expansion, new concept development goals, new products, new projects, or new ventures, customer satisfaction, staffing, training and development goals, goals relating to acquisitions, divestitures, affiliates and joint ventures. Business criteria may be measured on a consolidated basis, by department, group or business unit, or for specified subsidiaries or affiliates of the Company. The targeted level or levels of performance with respect to such business criteria may be established at such levels and in such terms as the Committee may determine, in its discretion, including in absolute terms, as a ratio, as a goal relative to performance in prior periods, or as a goal compared to the performance of one or more comparable companies or an index covering multiple companies.

(c) **Establishment of Performance Goals.** With respect to Performance-Based Awards, the Committee shall establish in writing (i) the performance goals applicable to a specified performance period, and such performance goals shall state, in terms of an objective formula or standard, the method for computing the amount of compensation payable to the participant if such performance goals are obtained and (ii) the individual employees or class of employees to which such performance goals apply; provided, however, that such performance goals shall be established in writing no later than ninety (90) days after the commencement of the applicable performance period (but in no event after twenty-five percent (25%) of such performance period has elapsed). Performance periods may be of any length, as specified by the Committee.
(d) Certification of Performance. No Performance-Based Awards shall be payable to or vest with respect to, as the case may be, any participant for a given period until there has been certified in writing by or on behalf of the Committee that the objective performance goals (and any other material terms) applicable to such period have been satisfied.

(e) Modification of Performance-Based Awards. With respect to any Awards or the cash denominated awards under Section 10(f) intended to qualify as Performance-Based Awards, after establishment of a performance goal, the Committee shall not revise such performance goal or increase the amount of compensation payable thereunder (as determined in accordance with Section 162(m) of the Code) upon the attainment of such performance goal. Notwithstanding the preceding sentence, the Committee may reduce or eliminate the number of shares of Common Stock or cash granted, vested or payable upon the attainment of such performance goal.

11. Foreign Laws. The Committee may grant Awards to individual participants who are subject to the tax and other laws of nations other than the United States, which Awards may have terms and conditions as determined by the Committee as necessary to comply with applicable foreign laws and local compensation customs and practices, and that may differ from those applicable to other participants. The Committee may take any action which it deems advisable to obtain approval of such Awards by the appropriate foreign governmental entity; provided, however, that no such Awards may be granted pursuant to this Section 11 and no action may be taken which would result in a violation of the Exchange Act or any other applicable law.

12. Certain Terminations of Employment; Forfeitures.

(a) Forfeiture of Unsettled Awards. Unless the Committee or any agreement relating to Awards under this Plan shall otherwise provide, a participant shall forfeit all Awards he or she holds at the time and which have not been settled under this Plan (other than fully vested Restricted Stock Awards and vested Stock Units that have been deferred at the election of the participant) if:

(i) the participant’s employment with the Company or with any Parent Corporation or Subsidiary Corporation is terminated for willful, deliberate, or gross misconduct in the performance of the participant’s duties to the Company, Parent Corporation or Subsidiary Corporation, as determined by the Committee in its good faith judgment, or any other event which constitutes “cause” under an employment agreement to which such participant is a party; or

(ii) following the participant’s termination of employment with the Company or with any Parent Corporation or Subsidiary Corporation and for a period of one (1) year thereafter, the participant engages in any business or enters into any employment relationship in violation of any non-competition obligation which such participant has to the Company, a Parent Corporation or Subsidiary Corporation or in violation of any restriction to which the participant is subject on, directly or indirectly, soliciting the employment of or any business from, or employing or doing business with, any of the employees or former employees of the Company (or any Parent Corporation or Subsidiary Corporation) or any customer or supplier to the Company (or any Parent Corporation or Subsidiary Corporation), or any other party with which the Company (or any Parent Corporation or Subsidiary Corporation) has a business relationship (including any such obligation or restriction contained in any agreement pursuant to which any Award is provided or any other agreement), and the Committee in its sole discretion has determined the results of such violation to have been injurious to the Company’s business interests.

The activities described in (i) and (ii) above are hereafter referred to as “Injurious Conduct”.

(b) Effect on Settled Awards. A forfeiture of Awards provided by Section 12(a) upon the Committee determining that a participant has engaged in Injurious Conduct during the course of his employment or during the one (1) year period following his or her termination of employment, shall not
relieve the participant of any liability he or she may have to the Committee as a result of engaging in the Injurious Conduct. In addition, the Committee may provide, in any Award agreement, for a forfeiture of gains previously realized upon exercise, lapse of restrictions or settlement of an Award (commonly referred to as a “clawback”) in the event of Injurious Conduct by a participant during employment or a specified period following employment.

(c) **Timing.** The Committee shall exercise the right of forfeiture provided to the Company in this Section 12 within ninety (90) days after the discovery of the activities giving rise to the Company’s right of forfeiture, which activities must have occurred no later than twelve (12) months after the participant’s termination of employment.

(d) **Determination from the Committee.** A participant may make a request to the Committee in writing for a determination regarding whether any proposed business or activity would constitute Injurious Conduct. Such request shall fully describe the proposed business or activity. The Committee shall respond to the participant in writing and the Committee’s determination shall be limited to the specific business or activity so described.

(e) **Condition Precedent.** Unless the Committee or any agreement relating to Awards under this Plan shall otherwise provide, all Awards shall be considered awarded under this Plan subject to the applicability of this Section 12.

(f) **Enforceability.** The purpose of this Section 12 is to protect the Company (and any Parent Corporation and Subsidiary Corporations) from Injurious Conduct. To the extent that this Section 12 is not fully enforceable as written, the unenforceable provisions shall be modified so as to provide the Company with the fullest protection permitted by law.

13. **Adjustment Provisions.** Awards granted under the Plan and any agreements evidencing such Awards, the maximum number of shares of Common Stock deliverable under all Awards stated in Section 5(a), the maximum number of shares of Common Stock available for Restricted Stock Awards and Stock Units under Section 5(a), and the maximum number of shares of Common Stock with respect to which Awards may be granted to or measured with respect to any one person during any period stated in Section 5(a) shall be subject to adjustment or substitution, as determined by the Committee in its sole discretion, as to the number, price or kind of a share of Common Stock or other consideration subject to such Awards or as otherwise determined by the Committee to be equitable (i) in the event of changes in the outstanding Common Stock or in the capital structure of the Company by reason of stock or extraordinary cash dividends, stock splits, reverse stock splits, recapitalizations, reorganizations, mergers, consolidations, combinations, exchanges, spin-offs, dividends in kind, or other relevant changes in capitalization, or (ii) in the event of any change in applicable laws or any change in circumstances which results in or would result in any substantial dilution or enlargement of the rights granted to, or available for, participants, or which otherwise warrants equitable adjustment because it interferes with the intended operation of the Plan. With respect to outstanding Awards, each participant has a legal right to the equitable adjustment provided hereunder, in order to preserve without enlarging the participant’s rights with respect to such Awards. Any adjustment in Incentive Stock Options under this Section 13 shall be made only to the extent not constituting a “modification” within the meaning of Section 424(h)(3) of the Code, and any adjustments under this Section 13 shall be made in a manner which does not adversely affect the exemption provided pursuant to Rule 16b-3 under the Exchange Act and which otherwise is permissible under Code Section 409A. Further, with respect to Awards intended to qualify as “performance-based compensation” under Section 162(m) of the Code, such adjustments or substitutions shall be made only to the extent that the Committee determines that such adjustments or substitutions may be made without causing the Company to be denied a tax deduction on account of Section 162(m) of the Code. The Company shall give each participant notice of an adjustment hereunder and, upon notice, such adjustment shall be conclusive and binding for all purposes.
14. Nontransferability. Each Award granted under the Plan to a participant (other than unrestricted Stock Awards and vested Restricted Stock Awards) shall not be transferable otherwise than by will or the laws of descent and distribution, and shall be exercisable, during the participant’s lifetime, only by the participant. In the event of the death of a participant, each Stock Option or Stock Appreciation Right theretofore granted to him or her shall be exercisable during such period after his or her death as the Committee shall in its discretion set forth in such option or right at the date of grant and then only by the executor or administrator of the estate of the deceased participant or the person or persons to whom the deceased participant’s rights under the Stock Option or Stock Appreciation Right shall pass by will or the laws of descent and distribution or beneficiary designation. Notwithstanding the foregoing, at the discretion of the Committee, an award of an Award other than an Incentive Stock Option may permit the transferability of an Award by a participant solely to the participant’s spouse, siblings, parents, children and grandchildren or trusts for the benefit of such persons or partnerships, corporations, limited liability companies or other entities owned solely by such persons, including trusts for such persons, subject to any restriction included in the grant of the Award.

15. Other Provisions. The grant of any Award under the Plan may also be subject to such other provisions (whether or not applicable to the Award granted to any other participant) as the Committee determines appropriate, including, without limitation, provisions for the forfeiture of, or restrictions on resale or other disposition of, Common Stock acquired under any form of Award, provisions for the acceleration of exercisability or vesting of Awards (subject to Section 19(a)), performance conditions other than those imposed under Section 10, or provisions to comply with federal and state securities laws, or understandings or conditions as to the participant’s employment in addition to those specifically provided for under the Plan.

16. Fair Market Value. For purposes of this Plan and any Awards awarded hereunder, Fair Market Value on any given date means the fair market value of the shares of Common Stock determined by such methods or procedures as shall be established from time to time by the Board of Directors. Unless otherwise determined by the Board of Directors, (i) if the Common Stock is listed on a national securities exchange or is quoted in the National Market System of the National Association of Securities Dealers Automated Quotation System (“NASDAQ”) on a last sale basis, the average of the opening price and the closing price reported as having occurred on such date, or, if there is no sale on such date, then on the last preceding date on which such a sale was reported, or (ii) if the Common Stock is not listed on a national securities exchange nor quoted in NASDAQ on a last sale basis, the amount determined by the Committee (or in accordance with procedures approved by the Committee) to be the fair market value based upon a good faith attempt to value the Common Stock accurately.

17. Withholding. All payments or distributions of Awards made pursuant to the Plan shall be net of any amounts required to be withheld pursuant to applicable federal, state and local tax withholding requirements. If the Company proposes or is required to distribute Common Stock pursuant to the Plan, it may require the recipient to remit to it or to the corporation that employs such recipient an amount sufficient to satisfy such tax withholding requirements prior to the delivery of any certificates for such Common Stock. In lieu thereof, the Company or the employing corporation shall have the right to withhold the amount of such taxes from any other sums due or to become due from such corporation to the recipient as the Committee shall prescribe. The Committee may, in its discretion and subject to such rules as it may adopt (including any as may be required to satisfy applicable tax and/or non-tax regulatory requirements), require, or permit an election by, an optionee or award or right holder to pay all or a portion of the federal, state and local withholding taxes arising in connection with any Award consisting of shares of Common Stock by having the Company withhold shares of Common Stock having a Fair Market Value equal to the amount of tax to be withheld, such tax calculated at minimum statutory withholding rates.
18. **Employment Rights.** Neither the Plan nor any action taken hereunder shall be construed as giving any participant the right to be retained in the employ or service of the company or any of its subsidiaries or affiliates.

19. **Tax Compliance**

   (a) **Certain Limitations on Awards to Ensure Compliance with Section 409A.** For purposes of this Plan, references to an Award term or event (including any authority or right of the Company or a participant) being “permitted” under Section 409A shall mean, for a 409A Award, that the term or event will not cause the participant to be liable for payment of interest or a tax penalty under Section 409A and, for a Non-409A Award, that the term or event will not cause the Award to be treated as subject to Section 409A. Other provisions of the Plan notwithstanding, the terms of any 409A Award and any Non-409A Award, including any authority of the Company and rights of the participant with respect to the Award, shall be limited to those terms permitted under Section 409A, and any terms not permitted under Section 409A shall be automatically modified and limited to the extent necessary to conform with Section 409A. For this purpose, other provisions of the Plan notwithstanding, the Company shall have no authority to accelerate distributions relating to 409A Awards in excess of the authority permitted under Section 409A, any distribution subject to Section 409A(a)(2)(A)(i) (separation from service) to a “key employee” as defined under Section 409A(a)(2)(B)(i) shall not occur earlier than the earliest time permitted under Section 409A(a)(2)(B)(i), any distribution triggered by a participant’s termination of employment and intended to qualify under Section 409A(a)(2)(B)(i) shall be made only at such time as the participant has had a “separation from service” within the meaning of Section 409A(a)(2)(A)(i), and any authorization of payment of cash to settle a Non-409A Award shall apply only to the extent permitted under Section 409A for such Award.

   (b) **Certain Terms Relating to Code Section 409A.** "409A Awards" means Awards that constitute a deferral of compensation under Code Section 409A and regulations thereunder. "Non-409A Awards" means Awards other than 409A Awards (including those exempt as “short-term deferrals” under Proposed Treasury Regulation § 1.409A-1(b)(4) and any successor regulation). Although the Committee retains authority under the Plan to grant Options, SARs and Restricted Stock on terms that will qualify those Awards as 409A Awards, Options, SARs, and Restricted Stock are intended to be Non-409A Awards unless otherwise expressly specified by the Committee.

   (c) **Unfunded Plan.** Participants shall have no right, title, or interest whatsoever in or to any investments which the Company may make to aid it in meeting its obligations under the Plan. Nothing contained in the Plan, and no action taken pursuant to its provisions, shall create or be construed to create a trust of any kind, or a fiduciary relationship between the Company and any participant, beneficiary, legal representative or any other person. To the extent that any person acquires a right to receive payments from the Company under the Plan (excluding Restricted Stock), such right shall be no greater than the right of an unsecured general creditor of the Company. All payments to be made hereunder shall be paid from the general funds of the Company and no special or separate fund shall be established and no segregation of assets shall be made to assure payment of such amounts except as expressly set forth in the Plan. The Plan is not intended to be subject to the Employee Retirement Income Security Act of 1974, as amended.

20. **No Fractional Shares.** No fractional shares of Common Stock shall be issued or delivered pursuant to the Plan or any Award. The Committee shall determine whether cash, or Awards, or other property shall be issued or paid in lieu of fractional shares or whether such fractional shares or any rights thereto shall be forfeited or otherwise eliminated.

21. **Duration, Amendment and Termination.** No Award shall be initially granted more than ten (10) years after the latest date upon which the Plan (including any amendment and restatement of the Plan) has been approved by shareholders, but Awards outstanding at that time shall remain outstanding and governed by the terms of the Plan. The Company may amend the Plan from time to time or suspend or
terminate the Plan at any time. However, no amendment of the Plan may be made without approval of holders of a majority of the voting power of the Common Stock (as defined in the Company’s Amended and Restated Certificate of Incorporation as in effect immediately after the Effective Date), voting together as a single class, if the amendment will: (i) increase the aggregate number of shares of Common Stock that may be delivered through Awards under the Plan; (ii) increase the maximum number of shares or cash that may be awarded to any participant under Section 5 hereof; (iii) change the types of business criteria on which Performance-Based Awards are to be based under the Plan; or (iv) modify the Plan so as to materially broaden eligibility for participation in the Plan; provided, however, that adjustments authorized under Section 13 are not subject to shareholder approval under this Section 21. Without the approval of shareholders, the Committee will not amend or replace previously granted Options or SARs in a transaction that constitutes a “repricing.” For this purpose, a “repricing” means: (1) amending the terms of an Option or SAR after it is granted to lower its exercise price; (2) any other action that is treated as a repricing under generally accepted accounting principles; and (3) canceling an Option at a time when its strike price is equal to or greater than the fair market value of the underlying Stock, in exchange for another Option, SAR, Restricted Stock, or other equity, unless the cancellation and exchange occurs in connection with a merger, acquisition, spin-off or other similar corporate transaction. A cancellation and exchange described in clause (3) of the preceding sentence will be considered a repricing regardless of whether the Option, Restricted Stock or other equity is delivered simultaneously with the cancellation, regardless of whether it is treated as a repricing under generally accepted accounting principles, and regardless of whether it is voluntary on the part of the Option holder. Adjustments to awards under Section 13 will not be deemed “repricings,” however.

22. Governing Law. This Plan, Awards granted hereunder and actions taken in connection herewith shall be governed and construed in accordance with the laws of the State of Delaware (regardless of the law that might otherwise govern under applicable Delaware principles of conflict of laws).

23. Effective Date. This Plan has been adopted by the Board of Directors of the Company and shall be effective as of the date of approval by the Company’s shareholders at the 2006 Annual Meeting of Shareholders, by the affirmative vote of a majority of the voting power present in person or by proxy and entitled to vote generally in the election of directors and entitled to vote on the matter of approval of this Plan. Such shareholder approval shall be a condition to the right of each participant to receive any Awards hereunder. Any Awards granted under the Plan prior to such shareholder approval shall be effective as of the date of grant (unless, with respect to any Award, the Committee specifies otherwise at the time of grant), but no such Award may be exercised or settled and no restrictions relating to any Award may lapse prior to such shareholder approval and, if such shareholder approval is not obtained as provided hereunder, any such Award shall be cancelled.
1. **Purposes.** The purpose of this 2006 Director Equity Compensation Plan (the “Plan”) is to serve as part of an appropriate and efficient package of compensation arrangements intended to attract, retain and fairly compensate individuals with the appropriate skills and qualifications to serve as directors of Magellan Health Services, Inc. (the “Company”) while increasing participating directors’ stock ownership in the Company and thereby further aligning their interests and those of the Company’s shareholders. The amount, timing and other terms of cash compensation that may be paid by the Company to directors are not governed by this Plan. In addition, adoption of this Plan shall not limit the authority of the Board to adopt other compensation programs in which directors may participate.

2. **Definitions.** In addition to the terms defined in Section 1, the following terms shall be defined as set forth below:

   (a) “Administrator” shall have the meaning set forth in Section 11.b.

   (b) “Annual Award Date” shall have the meaning set forth in Section 5.a.

   (c) “Annual Award” shall have the meaning set forth in Section 5.a.

   (d) “Black-Scholes Valuation” means the present value of an Option as of the date in question, calculated by means of the Black-Scholes option pricing model, so called, as calculated by a qualified financial analyst or compensation expert based on historical market price information and assumptions as to rates of interest and other factors which the Board believes are reasonable under the circumstances.

   (e) “Board” means the Board of Directors of the Company as then constituted.

   (f) “Change of Control” means the first to occur after the effective date of this Plan of any of the following events:

      (i) any “person,” as such term is used in Sections 3(a)(9) and 13(d) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), acquires Voting Stock (as defined below) and immediately thereafter is a “beneficial owner,” as such term is used in Rule 13d-3 promulgated under the Exchange Act, of 30% or more of the Voting Stock of the Company;

      (ii) the majority of the Board of Directors of the Company consists of individuals other than “Continuing Directors,” which shall mean the members of the Board on the effective date of the Plan; provided that any person becoming a director subsequent to the date hereof whose election or nomination for election was supported by two-thirds of the directors who then comprised the Continuing Directors, shall be considered to be a Continuing Director;

      (iii) the Board of Directors of the Company adopts and, if required by law or the certificate of incorporation of the Company, the shareholders approve the dissolution of the Company or a plan of liquidation or comparable plan providing for the disposition of all or substantially all of the Company’s assets, and all material conditions to such transactions have been satisfied;

      (iv) all or substantially all of the assets of the Company are disposed of pursuant to a merger, consolidation, share exchange, reorganization or other transaction unless the shareholders of the Company immediately prior to such merger, consolidation, share exchange, reorganization or other transaction beneficially own, directly or indirectly, in substantially...
the same proportion as they previously owned the Voting Stock or other ownership interests of the Company, a majority of the Voting Stock or other ownership interests of the entity or entities, if any, that succeed to the business of the Company; or

(v) the Company merges or combines with another company and, immediately after the merger or combination, the shareholders of the Company immediately prior to the merger or combination own, directly or indirectly, 50% or less of the Voting Stock of the successor company with the proportionate ownership of individual shareholders not substantially changed, provided that in making such determination there shall be excluded from the number of shares of Voting Stock held by such shareholders, but not from the Voting Stock of the successor company, any shares owned by affiliates of such other company who were not also affiliates of the Company prior to such merger or combination.

For purposes of this Section 2(f), the term “Voting Stock” shall mean the Company’s Ordinary Common Stock and any other capital stock which entitles the holder thereof to vote (either as part of a voting group or generally) in the election of directors.

(g) “Disability” means a Qualifying Director’s termination of service as a director of the Company due to physical or mental incapacity of long duration which renders such person unable to perform the duties of a director of the Company.

(h) “Fair Market Value” means, with respect to Shares, the fair market value of such Shares determined by such methods or procedures as shall be established from time to time by the Board. Unless otherwise determined by the Board, the Fair Market Value of a Share as of any given date means the average of the opening and closing prices of the Shares reported on the NASDAQ National Market for such date, or, if no Shares were traded on that date, on the next preceding day on which there was such a trade.

(i) “Mandatory Retirement” means the termination of a directors’ service in accordance with any mandatory retirement policy adopted by the Board and then in effect.

(j) “Option” means the right, granted to a Qualifying Director under Section 5, to purchase a specified number of Shares at the specified exercise price for a specified period of time under the Plan. All Options will be non-qualified stock options.

(k) “Restricted Shares” means Shares granted to a Qualifying Director under Section 5, subject to a risk of forfeiture and restrictions on transfer for a specified period as provided in Section 6.

(l) “Shares” means shares of Ordinary Common Stock of the Company or such other securities as may be substituted for Shares pursuant to Section 9.

(m) “Qualifying Annual Meeting” shall mean the annual meeting of shareholders held in 2006 or thereafter.

(n) “Qualifying Director” means a person who (i) is serving as a director of the Company at the close of business on the date of a “Qualifying Annual Meeting,” or is elected as a director of the Company after each such date and before the next following annual meeting of shareholders of the Company and is designated by the Board of Directors to participate in the Plan and (ii) has been designated by the Board of Directors as an “independent director” as determined for purposes of Article III, Section 3 of the Bylaws of the Company as from time to time in effect or, although not so designated, is not an officer or employee of the Company or any subsidiary of the Company and does not otherwise participate in the management of the Company and has been designated by the Board of Directors to participate in the Plan.
3. **Effective Date.** The Plan has been adopted by the Board and shall be effective as of the date of approval by the Company’s shareholders at the 2006 annual meeting of shareholders, by the affirmative vote of a majority of the voting power present in person or by proxy and entitled to vote on the matter of approval of this Plan. Such shareholder approval shall be a condition to the right of each participant to receive any awards hereunder.

4. **Participation.** Only Qualifying Directors shall be eligible to participate in the Plan.

5. **Award of Restricted Shares and Options.**
   a. **Time of Award.** Immediately following the date of each Qualifying Annual Meeting of the Company (each, an “Annual Award Date”), each Qualifying Director shall be issued by the Company, in consideration of the services to be provided by him or her as a director of the Company for the ensuing year, a number of Restricted Shares and Options determined in accordance with Section 5(b) (an “Annual Award”), subject to adjustment in accordance with Section 9; provided, however, that a lesser number of Restricted Shares and Options, as may be determined by the Board, may be issued to a Qualifying Director whose service as a director commences after a Qualifying Annual Meeting and before the next Qualifying Annual Meeting; and provided further, that the issuance of shares of Restricted Stock will be delayed for ten days, with the performance of services during such period being deemed payment of lawful consideration having a value at least equal to the par value of the Restricted Stock.
   b. **Determination of Awards.** The Annual Awards shall consist of: (i) 750 Restricted Shares, and (ii) a number of Options with an aggregate value, determined on the basis of a Black-Scholes Valuation as of the Annual Award Date, equal to the Fair Market Value on the Annual Award Date of 2,250 Shares. All such Options shall be awarded with an exercise price equal to 100% of the Fair Market Value of a Share as of the Annual Award Date and shall expire on the earlier of (i) the date which is ten (10) years following the Annual Award Date (or such earlier date as may be specified by the Board prior to award), or (ii) if not otherwise forfeited upon termination of service, one year after the Qualifying Director ceases to serve as a director of the Company for any reason.
   c. **Applicability of Restrictions.** The issuance of Restricted Shares and Options hereunder pursuant to each Annual Award shall be subject to the restrictions on transfer and ownership thereof provided by Section 6 of this Plan. In addition, the Company shall not be obligated to issue Shares except upon compliance with applicable provisions of law, including federal and state securities laws.
   d. **Issuance of Instruments.** Certificates representing Restricted Shares shall bear an appropriate legend referring to the terms, conditions and restrictions applicable to such Restricted Shares, the Company shall retain physical possession of the certificate, and the Qualifying Director shall have delivered a stock power to the Company, endorsed in blank, relating to the Restricted Shares. Upon the lapse of restrictions on the Restricted Shares, the Share certificate shall be released by the Company to the Qualifying Director with any legend relating to such restrictions removed. Options shall be evidenced by award notices in such form as may be adopted from time to time by the Administrator and shall bear an appropriate legend referring to the terms, conditions and restrictions applicable to such Options, until the lapse of such restrictions in accordance with the terms of this Plan.

6. **Restrictions on Ownership and Transfer of Restricted Shares and Options.** Prior to the vesting and lapse of restrictions on Restricted Shares and Options as provided in this Section 6, the Restricted Shares and Options comprising an Annual Award shall not be transferable by the recipient, except by will or the laws of descent and distribution, or to a beneficiary in the event of a Qualifying Director’s death.
and will not otherwise be subject to alienation, anticipation, encumbrance, garnishment, attachment, levy, execution or other legal or equitable process, nor subject to the debts, contracts, liabilities or engagement, or torts of any Qualifying Director or his or her beneficiary. Any attempt to alienate, sell, transfer, assign, pledge, garnish, attach or take any other action subject to legal or equitable process or encumber or dispose of any interest in the Plan shall be void. Such Restricted Shares and Options shall vest and become non-forfeitable in full at the close of business on the date which is one full year following the Annual Award Date, subject to the following:

a. In the event of a Change of Control of the Company or the termination of a Qualifying Director’s service as a director due to his or her death or Disability, the Annual Award, if not previously vested or forfeited, shall immediately vest and become non-forfeitable in full. Following the death or Disability of a Qualifying Director, his or her estate, heirs, distributees or personal representative shall succeed to all of the Qualifying Director’s right, title and interest in and to the Restricted Shares and Options.

b. In the event of termination of the Qualifying Director’s service as a director due to Mandatory Retirement, the award, if not previously vested or forfeited, shall immediately vest and become non-forfeitable in full.

c. Unless otherwise determined by the Board, an award of Restricted Shares and/or Options that has not vested in accordance with this Section 6 at or before the time of termination of the Qualifying Director’s service as a director for any reason other than as set forth in Section 6.a. and b. will cease to vest and will be forfeited upon such termination.

d. From and after the time vested in accordance with this Section 6, Restricted Shares and Options may only be sold or otherwise transferred in accordance with policies generally established by the Board with respect to sales of shares of the Company by directors of the Company and applicable securities laws.

e. Once granted to a Qualifying Director, Restricted Shares may be voted by the Qualifying Director (or his or her successor) without restriction by virtue of the Plan.

f. Once granted to a Qualifying Director, Restricted Shares shall, unless otherwise determined by the Board, be entitled to receive cash dividends which are not large, special and non-recurring and which are paid prior to the lapse of the risk of forfeiture on such Restricted Shares. Other dividends will be payable or not payable and subject to adjustment to the Restricted Shares in accordance with Section 9, with the resulting additional Restricted Shares subject to the same terms, including risk of forfeiture, as the Restricted Shares on which the dividend was paid.

g. Notwithstanding the foregoing vesting and forfeiture provisions, the Administrator may permit a Qualifying Director to transfer Options to trusts, limited liability companies, partnerships and other like entities solely for the purpose of estate planning, provided that any such transfer is consistent with the registration of any offer and sale of Shares related thereto on Form S-8, S-3 or other applicable registration form as may be used in connection with the Plan, and any such transferee is also subject to the restrictions to which the Qualifying Director is subject under the Plan. In addition, the foregoing vesting and forfeiture provisions shall not impair any change in or exchange of the shares occurring by reason of a merger, consolidation, recapitalization, reorganization or like transaction involving the Company.

7. Payment of Option Exercise Price. Prior to the exercise of an Option, the holder thereof shall have none of the rights of a shareholder of the Company. The exercise price of an Option shall be paid to the Company either in cash or by the surrender of Shares or the withholding of Shares from those deliverable upon exercise of the Option, or any combination thereof, or in such other lawful form or manner as may be established by the Administrator.
8. **Shares Available Under the Plan.** Subject to adjustment as provided in Section 9 below, the total number of Shares reserved and available for delivery under the Plan for awards shall be 120,000; provided, however, that no more than 15,000 Restricted Shares in the aggregate may be awarded under the Plan. The Shares delivered under the Plan may consist of authorized and unissued or treasury shares, and Shares underlying Restricted Shares or Options which are forfeited shall be available for future awards.

9. **Change in Capital Stock.** The total number and kind of shares which may be issued under the Plan and that are granted under Section 5 shall be appropriately adjusted for any change in the outstanding Shares through recapitalization, stock split, stock dividend, merger or consolidation in which the Company is the surviving corporation or similar transaction. In such case, the number of shares subject to outstanding Restricted Stock and Options, and related terms (including the exercise price of each Option) also shall be adjusted so as to prevent dilution or enlargement of the rights of participants. Such adjustments and the manner of application thereof shall be determined by the Board in its discretion.

10. **Nonassignability.** No rights under this Plan shall be assignable or transferable by a Qualifying Director other than as set forth in the first paragraph of Section 6 or in Section 6.g.

11. **Administration.**

   a. **Authority.** The Board and the Administrator, acting under the direction of the Board, shall administer and interpret this Plan in accordance with its terms, and shall have all powers necessary to accomplish such purpose. The Board may delegate any or all of its functions to a committee of the Board, provided that the Board shall approve the form and amount of compensation to directors under any provision of the Plan. The Administrator may perform any function of the Board under the Plan, except for adopting material amendments to the Plan and any other function from time to time specifically reserved by the Board to itself. The Board and the Administrator may each appoint agents and delegate thereto powers and duties under the Plan, except as otherwise limited by the Plan.

   b. **Administrator.** The Administrator shall be the chief legal officer of the Company, or, if that officer is unavailable, the chief financial officer; provided, however, that the Board may designate a different individual or committee to serve as Administrator.

12. **Changes to the Plan and Awards.** The Board may amend, suspend, discontinue or terminate the Plan or the award of Restricted Shares and Options under the Plan, without the consent of any other party, including the shareholders of the Company; provided that any amendment shall be subject to shareholder approval if and to the extent then required under applicable rules of the NASDAQ National Market or any other stock exchange or automated quotation system upon which the Shares may then be listed or quoted; and provided further that no such action may materially impair the rights of a recipient of an award previously made without the consent of such recipient. Without the prior approval of the shareholders of the Company, the Board may not amend or replace previously granted Options in a transaction that constitutes a “repricing.” For this purpose, “repricing” means: (i) amending the terms of an Option after it is granted to lower its exercise price; (ii) any other action that is treated as a repricing under generally accepted accounting principles; and (iii) canceling an Option at a time when its exercise price is equal to or greater than the fair market value of the underlying Shares, in exchange for another Option, Restricted Shares or other equity, unless the cancellation and exchange occurs in connection with a merger, acquisition, spin-off or other similar corporate transaction. Adjustments to Restricted Stock and Options under Section 9 will not be deemed repricings, however.
13. **Governing Law.** This Plan, awards granted hereunder and actions taken in connection herewith shall be governed and construed in accordance with the laws of the State of Delaware (regardless of the law that might otherwise govern under applicable Delaware principles of conflicts of laws).

14. **Tax Compliance.**

   (a) **Certain Terms Relating to Code Section 409A.** “409A Awards” means awards that constitute a deferral of compensation under Section 409A of the Internal Revenue Code of 1986, as amended, and regulations thereunder. “Non-409A Awards” means an award other than 409A Awards (including those exempt as “short-term deferrals” under Proposed Treasury Regulation § 1.409A-1(b)(4) and any successor regulation). Although the Board retains authority under the Plan to grant Options and Restricted Shares on terms that will qualify those awards as 409A Awards, Options and Restricted Shares are intended to be Non-409A Awards unless otherwise expressly specified by the Committee.

   (b) **Compliance with Code Section 409A.** For purposes of this Plan, references to an award term or event (including any authority or right of the Company or a participant) being “permitted” under Section 409A shall mean (i) for a 409A Award, that the term or event will not cause the participant to be liable for payment of interest or a tax penalty under Section 409A and (ii) for a Non-409A Award, that the term or event will not cause the award to be treated as subject to Section 409A. Other provisions of the Plan notwithstanding, the terms of any 409A Award and any Non-409A Award, including any authority of the Company and rights of the participant with respect to the award, shall be limited to those terms permitted under Section 409A, and any terms not permitted under Section 409A shall be automatically modified and limited to the extent necessary to conform with Section 409A.
1. PURPOSE. The purpose of the Magellan Health Services, Inc. 2006 Employee Stock Purchase Plan (the “Plan”), is to provide employees of Magellan Health Services, Inc. (the “Company”) and its subsidiary companies with an opportunity to be compensated through the benefits of stock ownership and to acquire an interest in the Company through the purchase of Common Stock of the Company. It is the intention of the Company to have the Plan qualify as an “employee stock purchase plan” under Section 423 of the Internal Revenue Code of 1986 (the “Code”). The provisions of the Plan shall, accordingly, be construed so as to extend and limit participation in a manner consistent with the requirements of that section of the Code.

2. DEFINITIONS.
   (a) “Base Pay” means the compensation payable to an employee by the Company or a designated subsidiary (as defined in Code Section 424(f)) (a “subsidiary”), calculated at that employee’s base salary or standard hourly rate of compensation, but excluding overtime, commissions, shift differential, incentive bonus compensation and compensation payable under any deferred compensation or other fringe benefit plan.
   (b) “Employee” means for each Offering Period (as defined in Section 4) any person who is employed by the Company or by any subsidiary of the Company designated from time to time by the Committee (as defined in Section 13) to participate in such Offering Period.

3. ELIGIBILITY.
   (a) Any Employee who shall be employed on the 60th day preceding the Offering Date of an Offering Period shall be eligible to participate in the Plan for such Offering Period. Notwithstanding the foregoing, the Committee, in its sole discretion, may credit the employment service of persons employed by a business acquired by the Company or by any subsidiary thereof for the purpose of satisfying the 60-day rule herein.
   (b) Any provision of the Plan to the contrary notwithstanding, no Employee shall be granted an option:
      (i) If, immediately after the grant such Employee would own shares, and/or hold outstanding options to purchase stock, possessing 5% or more of the total combined voting power or value of all classes of shares of the Company or of any subsidiary of the Company; or
      (ii) Which permits his rights to purchase shares under all employee stock purchase plans of the Company and its subsidiaries to accrue at a rate which exceeds $25,000 of the fair market value of the shares (determined at the time such option is granted) for each calendar year in which such stock option is outstanding at any time.

4. OFFERING PERIODS. The Committee shall establish the Offering Periods under the Plan which shall be of not less than three months nor more than twelve months duration each, the first of which shall not begin before this Plan is approved by the shareholders of the Company, and the last of which shall end not later than December 31, 2010. The beginning date (the “Offering Date”) and the ending date (the “Termination Date”) of each Offering Period shall be set in advance of each Offering Period by the Committee.
5. PARTICIPATION. An eligible Employee may become a participant only by completing an election notice provided by the Company and filing it with the designated representative of the Company no later than the date specified by the Company in the election notice form.

Unless otherwise adjusted in accordance with rules established by the Committee in its sole discretion, payroll deductions for a participant with respect to an Offering Period shall commence with the first pay date beginning on or after the Offering Date, and shall end with the last pay date ending on or before the Termination Date, unless sooner terminated by the participant as provided in Section 10. All Employees granted options under the Plan shall have the same rights and privileges, except that the amount of stock which may be purchased under such option may vary in a uniform manner as described in Section 7.

6. METHOD OF PAYMENT. Payments for shares under the Plan may be made only by payroll deductions, as follows:

(a) If a participant wishes to participate in the Plan, then at the time he files his election notice, he shall elect to have deductions made from his Base Pay at a rate, expressed as a percentage, not to exceed 10% of his annualized Base Pay as of the Offering Date. Any or all amounts withheld during the one-month period immediately preceding the Termination Date in any Offering Period may be applied to the purchase of shares on the Termination Date or to the purchase of shares offered for the next subsequent Offering Period in a manner as may be determined by the Committee, in its sole discretion, but only if such application is administered consistently among all participants during such Offering Period.

(b) All payroll deductions made for a participant shall be credited to his account under the Plan. A participant may not make any separate cash payment into such account. A participant’s account shall be no more than a bookkeeping account maintained by the Company, and neither the Company nor any subsidiary shall be obligated to segregate or hold in trust or escrow any funds in a participant’s account.

(c) A participant’s election to have deductions made from his Base Pay shall be effective for all pay dates occurring during the Offering Period which commences immediately following the filing, in accordance with Section 5, of the participant’s election notice and for each subsequent Offering Period until such election is modified or revoked by the participant or until such participant no longer meets the eligibility requirements of Section 3(a). A participant may discontinue his participation in the Plan as provided in Section 10.

A participant may elect to change the rate of payroll deductions at such times and in accordance with such rules as may be prescribed by the Committee; any such change in the rate of payroll deductions shall be applicable only with respect to Offering Periods commencing after a participant files with the Committee an election notice requesting such change.

7. GRANTING OF OPTION.

(a) Subject to any adjustment under Sections 12 or 17, on the Offering Date for each Offering Period, a participant shall be granted an option to purchase a number of whole shares determined by dividing the amount to be withheld for participation in the Plan and applied to such Offering Period by the option price per share of Common Stock determined in accordance with Section 7(b).

(b) The option price per share of shares purchased with payroll deductions for a participant will be equal to the 95% of the closing price of the Common Stock on the Association of Securities Dealers Automatic Quotation System (NASDAQ) on the Termination Date. If no shares are traded on any such exchange (or any other national exchange) on either such date, such price shall be determined on the last trading date for such shares immediately preceding the Offering Date or the
8. EXERCISE OF OPTION. Unless a participant gives written notice of withdrawal pursuant to Section 10(a) or such participant’s payroll deductions are returned in accordance with Section 10(c), his option for the purchase of shares during an Offering Period with payroll deductions will be exercised automatically for him on the Termination Date of that Offering Period. The automatic exercise shall, subject to Sections 12 and 17, be for the purchase of the maximum number of full shares subject to his option which the sum of payroll deductions credited to the participant’s account (without interest) on the Termination Date can purchase at the option price.

9. DELIVERY. As promptly as practicable after the end of an Offering Period, the Company will deliver the shares purchased upon the exercise of the option to a designated broker selected by the Company to administer and hold shares in individual accounts established for the benefit of each participant. The Committee, in its sole discretion, may establish procedures to permit a participant to receive such shares directly. Amounts credited to the participant’s account in excess of the amount necessary to pay the option price for the maximum number of full shares subject to his option shall either be refunded to the participant or credited to the participant’s account for the next subsequent Offering Period as may be determined by the Committee, in its sole discretion.

10. WITHDRAWAL.

   (a) A participant may withdraw payroll deductions credited to his account under the Plan by giving written notice to the representative of the Company designated on the election notice form. A participant may withdraw amounts credited to his account at any time prior to the first day of the calendar month that includes the Termination Date or such later date as may be established by the Committee in its sole discretion. All of the participant’s payroll deductions credited to his account will be paid to him (without interest) promptly after receipt of his notice of withdrawal, and no further deductions will be made from his pay during that Offering Period.

   (b) A participant’s withdrawal will not limit his eligibility to participate in any similar plan which may hereafter be adopted by the Company or in any subsequent Offering Period.

   (c) Upon termination of the participant’s employment during an Offering Period for any reason, including death or retirement, the payroll deductions credited to his account for such period (without interest) will be returned to him or, in the case of his death, to the person or persons entitled thereto under Section 14. Notwithstanding the foregoing, the payroll deductions credited to the account of any participant whose employment is terminated during the calendar month that includes the Termination Date shall not be returned but shall instead be used to purchase shares in accordance with Section 8.

11. NO INTEREST. No interest shall be accrued or payable with respect to amounts in a participant’s account.

12. STOCK.

   (a) The shares of Common Stock to be sold to participants under the Plan may, at the election of the Company, be either treasury shares or shares originally issued for such purpose. The maximum number of shares which shall be made available for sale under the Plan shall be 100,000 shares and the maximum number of shares available for sale in each Offering Period shall be determined by the Committee in its sole discretion, subject in each case to adjustment upon changes in capitalization of the Company as provided in Section 17. If the total number of shares for which options are to be exercised for an Offering Period in accordance with Section 8 exceeds the number of shares then available under the Plan for such Offering Period, the Company shall make a pro rata allocation of
the shares available based on a fraction, the numerator of which shall be the number of shares with respect to which a participant has an option to purchase for an Offering Period and the denominator of which shall be the number of shares available for purchase, with rounding down for each participant to the nearest whole number.

(b) A participant will have no interest in shares covered by an option until such option has been exercised.

13. ADMINISTRATION. The Plan shall be administered by a Committee (the “Committee”) consisting of not less than three members who shall be appointed by the Chief Executive Officer of the Company. Each member of the Committee shall be either a director, an officer, or an employee of the Company or of a subsidiary thereof. The Committee shall be vested with full authority to make, administer, and interpret such rules and regulations as it deems necessary to administer the Plan, and any determination, decision, or action of the Committee in connection with the construction, interpretation, administration, or application of the Plan shall be final, conclusive, and binding upon all participants and all persons claiming under or through any participant.

14. DESIGNATION OF BENEFICIARY. A participant may file a written designation of a beneficiary who is to receive any shares or cash to the participant’s credit under the Plan in the event of such participant’s death before, on, or after the Termination Date but prior to the delivery of shares and, if applicable, cash. Such designation of beneficiary may be changed by the participant at any time by written notice. Upon the death of a participant and upon receipt by the Company of proof of the identity and existence at the participant’s death of a beneficiary validly designated by him under the Plan, the Company shall deliver such shares or cash to the account of such beneficiary. In the event of the death of a participant and in the absence of a beneficiary validly designated under the Plan who is living at the time of such participant’s death, the Company shall deliver such shares or cash to the account of the executor or administrator of the estate of the participant, or if no such executor or administrator has been appointed (to the knowledge of the Company) the Company, in its discretion, may deliver such shares or cash to the account of the spouse or to any one or more dependents or relatives of the participant, or if no spouse, dependent, or relative is known to the Company, then to the account of such other person as the Company may designate. No designated beneficiary shall, prior to the death of the participant by whom he has been designated, acquire any interest in the shares or cash credited to the participant under the Plan.

15. TRANSFERABILITY. Neither payroll deductions credited to a participant’s account nor any rights with regard to the exercise of an option or to receive shares under the Plan may be assigned, transferred, pledged, or otherwise disposed of in any way by the participant. Any such attempted assignment, transfer, pledge, or other disposition shall be without effect, except that the Company may treat such act as an election to withdraw funds in accordance with Section 10.

16. USE OF FUNDS. All payroll deductions received or held by the Company under the Plan may be used by the Company for any corporate purpose.

17. ADJUSTMENTS UPON CHANGES IN CAPITALIZATION. In the event that the outstanding shares of Common Stock of the Company are hereafter increased or decreased or changed into or exchanged for a different number or kind of shares or other securities of the Company by reason of a recapitalization, reclassification, stock split, combination of shares, or dividend payable in shares of Common Stock, an appropriate adjustment shall be made by the Committee to the number and kind of shares as to which outstanding options shall be exercisable and to the option price. No fractional shares shall be issued or optioned in making the foregoing adjustments. All adjustments made by the Committee under this paragraph shall be conclusive and binding on all participants and all persons claiming under or through any participant.
Subject to any required action by the stockholders, if the Company shall be a party to any reorganization involving a merger, consolidation, acquisition of the stock or acquisition of the assets of the Company, the Committee in its discretion may declare (a) that all options granted hereunder are to be terminated after giving at least ten days’ notice to holders of outstanding options, or (b) that any option granted hereunder shall pertain to and apply with appropriate adjustment as determined by the Committee to the securities of the resulting corporation to which a holder of the number of shares of Common Stock subject to the option would have been entitled. The adoption of a plan of dissolution or liquidation by the Board of Directors and stockholders of the Company shall cause every option outstanding hereunder to terminate on the fifteenth day thereafter, except that, in the event of the adoption of a plan of dissolution or liquidation in connection with a reorganization as provided in the preceding sentence, options outstanding hereunder shall be governed by and shall be subject to the provisions of the preceding sentence.

Any issue by the Company of stock of any class, or securities convertible into shares of stock of any class, shall not affect, and no adjustment by reason thereof shall be made with respect to, the number or price of shares of Common Stock subject to any option, except as specifically provided otherwise in this Section 17. The grant of an option pursuant to the Plan shall not affect in any way the right or power of the Company to make adjustments, reclassifications, reorganizations or changes of its capital or business structure or to merge or to consolidate or to dissolve, liquidate or sell, or transfer all or any part of its business or assets.

18. AMENDMENT OR TERMINATION. The Board of Directors of the Company may at any time terminate or amend the Plan. No such termination can affect options previously granted and no amendment can make any change in any option theretofore granted which would adversely affect the rights of any participant. No amendment can be made without prior approval of the stockholders of the Company if such amendment would:

(a) Require the sale of more shares than are authorized under Section 12; or

(b) Permit payroll deductions or cash payments at a rate in excess of 10% of a participant’s Base Pay.

19. NOTICES. All notices or other communications by a participant to the Company under or in connection with the Plan shall not be deemed to have been duly given until actually received by the representative of the Company designated on the election notice form provided in accordance with Section 5.

20. PAYEE. If (i) the Company utilizes a designated broker to administer and hold in individual accounts the shares purchased by the participants, (ii) the Company subsequently cannot ascertain the whereabouts of a participant whose account is held with the designated broker, (iii) after three years from the date of the last purchase by such participant, a notice of such account balance and pending action under this section is mailed to the last known address of such person, as shown on the records of the designated broker or the Company, and (iv) within three months after such mailing, such person has not made written claim therefor, then the Committee may direct that such account balance (including both shares and withholdings) otherwise due to such person be canceled and returned to the Company. Upon such cancellation, the Company or the designated broker shall have no further liability therefor, except that, in the event such person, within one year of the date of the notice referred to in (iii) above, notifies the Company or the broker of his whereabouts and requests the amounts due to him under the Plan, the number of shares (as may be adjusted to reflect any extraordinary corporate event or recapitalization) together with any dividends or other accretions thereon and the amount of withholdings contained in such account so canceled shall be delivered to him as provided herein by the Plan.
AMENDMENT TO EMPLOYMENT AGREEMENT

This Amendment to Employment Agreement between Magellan Health Services, Inc. (“Employer”) and ("Employee") entered into on this day of , 2006.

WHEREAS, Employer and Employee desire to amend the terms of the Employment Agreement currently in effect between Employer and Employee (the “Employment Agreement”).

NOW THEREFORE, Employer or Employee agree that the Employment Agreement is hereby amended as follows:

I. New Change in Control Provisions — Add the following new paragraphs:

1. Termination Without Cause by the Company or With Good Reason By Executive In connection With, Or Within Two Years After, A Change In Control: If Employer terminates this Agreement and Employee’s employment without cause, or if Employee terminates this Agreement and Employee’s employment with Good Reason, in connection with a Change in Control (as defined below) (whether before or at the time of such Change in control) or within two years after a change in Control, Employee shall receive the following, in lieu of the amounts and benefits described in Section 6:

   (i)   Base Salary through the date of termination;

   (ii)  pro-rata Target Bonus for the year in which termination occurs, payable in a single installment immediately after termination;

   (iii) 2 times the sum of (a) Base Salary plus (b) Target bonus, payable in a single cash installment immediately after termination;

   (iv) if employee elects COBRA coverage for health, dental and vision benefits, Employer shall pay Employer’s contributions for health insurance and Employee shall pay Employee’s contributions rate for health, dental and vision insurance for up to eighteen (18) months after termination.

   (v)    any other amounts earned, accrued or owing to Executive but not yet paid;

   (vi)   other payments, entitlements or benefits, if any, that are payable in accordance with applicable plans, programs, arrangements or other agreements of the company or any affiliate; and

   (vii)  all stock options granted to Employee from January 4, 2004 and prior to March 10, 2005 shall vest and become immediately exercisable.

Exhibit 10.4
2. **Definitions:**

   A. **Change in Control:**

   A “Change in Control” of the Company shall mean the first to occur after the date hereof of any of the following events:

   (i) any “person,” as such term is used in Sections 3(a)(9) and 13(d) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), becomes a “beneficial owner,” as such term is used in Rule 13d-3 promulgated under the Exchange Act, of 51% or more of the Voting Stock (as defined below) of the Company;

   (ii) the majority of the Board of Directors of the Company consists of individuals other than “Continuing Directors,” which shall mean the members of the Board on the date hereof, provided that any person becoming a director subsequent to the date hereof whose election or nomination for election was supported by a vote of the directors who then comprised the Continuing Directors, shall be considered to be a Continuing Director;

   (iii) the Board of Directors of the Company adopts and, if required by law or the certificate of incorporation of the Corporation, the shareholders approve the dissolution of the Company or a plan of liquidation or comparable plan providing for the disposition of all or substantially all of the Company’s assets;

   (iv) all or substantially all of the assets of the Company are disposed of pursuant to a merger, consolidation, share exchange, reorganization or other transaction unless the shareholders of the Company immediately prior to such merger, consolidation, share exchange, reorganization or other transaction beneficially own, directly or indirectly, in substantially the same proportion as they previously owned the Voting Stock or other ownership interests of the Company, 51% of the Voting Stock or other ownership interests of the entity or entities, if any, that succeed to the business of the Company; or

   (v) the Company merges or combines with another company and, immediately after the merger or combination, the shareholders of the Company immediately prior to the merger or combination own, directly or indirectly, 50% or less of the Voting Stock of the successor company, provided that in making such determination there shall be excluded from the number of shares of Voting Stock held by such shareholders, but not from the Voting
Stock of the successor company, any shares owned by Affiliates of such other company who were not also Affiliates of the Company prior to such merger or combination.

B. “Cause” in connection with a Change in Control shall mean:

(i) Employee is convicted of (or pleads guilty or nolo contendere to) a felony or a crime involving moral turpitude;

(ii) Employee’s commission of an act of fraud or dishonesty involving his or her duties on behalf of the Company;

(iii) Employee’s willful failure or refusal to faithfully and diligently perform duties lawfully assigned to Employee as an officer or employee of the Company or other willful breach of any material term of any employment agreement at the time in effect between the Company and Employee; or

(iv) Employee’s willful failure or refusal to abide by the Company’s policies, rules, procedures or directives, including any material violation of the Company’s Code of Ethics.

C. “Good Reason” shall mean:

(i) a reduction in Employee’s salary in effect at the time of a Change in Control, unless such reduction is comparable in degree to the reduction that takes place for all other employees of the Company of comparable rank, or a reduction in Employee’s target bonus opportunity for the year in which or any year after the year in which the Change of Control occurs from Employee’s target bonus opportunity for the year in which the Change of Control occurs (if any) as established under any employment agreement Employee has with the Company or any bonus plan of the Company applicable to Employee (or, if no such target bonus opportunity has yet been established for Employee under a bonus plan applicable to Employee for the year in which the Change of Control has occurred, the target bonus opportunity so established for Employee for the immediately preceding year, if any);

(ii) a material diminution in Employee’s position, duties or responsibilities as in effect at the time of a Change in Control, or the assignment to Employee of duties which are materially inconsistent with such position, duties and authority, unless in either case such change is made with the consent of the Employee; or

(iv) the relocation by more than 50 miles of the offices of the Company which constitute at the time of the Change in Control Employee’s principal location
D. “Company” shall include any entity that succeeds to all or substantially all of the business of the Company,

E. “Affiliate” of a person or other entity shall mean a person or other entity that directly or indirectly controls, is controlled by, or is under common control with the person or other entity specified,

F. “Voting Stock” shall mean any capital stock of any class or classes having general voting power under ordinary circumstances, in the absence of contingencies, to elect the directors of a corporation and reference to a percentage of Voting Stock shall refer to such percentage of the votes that all such Voting Stock is entitled to cast.

3 Tax Gross-Up. The following provisions shall apply with respect to any excise tax imposed under Section 4999 of the Internal Revenue Code as amended (the “Code”), (the “Excise Tax”):

a. If any of the payments or benefits received or to be received by Employee in connection with a Change in Control or Employee’s termination of employee (whether pursuant to the terms of this Agreement or any other plan, arrangement of agreement with the Company, any person whose actions result in a Change on Control of the Company or any person affiliated with the Company or such person (the “Total Payments”)) will be subject to the Excise Tax, the Company shall pay to Employee an additional amount (the “Gross-Up Payment”) such that the net amount retained by Employee after payment of (a) the Excise Tax, if any, on the Total Payments and (b) any Excise Tax and income tax due in respect of the Gross-Up Payment, shall equal the Total Payments. Such payment shall be made in a single lump sum within 10 days following the date of a determination that only such payment is required.

b. For purposes of determining whether any of the Total payments will be subject to Excise Tax and the amount of such Excise Tax, (i) any Total Payments shall be treated as “parachute payments” (within the meaning of Section 280G(b)(2) of the Code) unless, in the opinion of tax counsel selected by the Company and reasonably acceptable to Employee, such payments or benefits (in whole or in part) should not constitute parachute payments, including by reason of Section 280G(b)(4) of the Code, and all “excess parachute payments” (within the meaning of Section 280G(b)(1) of the Code) shall be treated as subject to the Excise Tax unless, in the opinion of such tax counsel, such excess parachute payments (in whole or in part) represent reasonable compensation for services actually rendered.
(within the meaning of Section 280G(b) (4) (B) of the Code), or are otherwise not subject to the Excise Tax, and (ii) the value of any noncash benefits or any deferred payment or benefit shall be determined by the Company’s independent auditors in accordance with the principles of Section 280G(d) (3) of the Code. For purposes of determining the amount of the Gross-Up payment, Employee shall be deemed to pay federal income and employment taxes at the highest marginal rate of federal income and employment taxation in the calendar year in which the Gross-Up Payment is to be made and state and local income and employment taxes at the highest marginal rate of taxation in the state and locality of Employee’s residence on the date of termination of employment (or such other time as hereinafter described), net of the maximum reduction in federal income or employment taxes which could be obtained from deduction of such state and local taxes.

In the event that the Excise Tax is subsequently determined to be less than the amount taken into account hereunder at the time of termination of Employee’s employment (or such other time as is hereinafter described), Employee shall repay to the Company, at the time that the amount of such reduction in Excise Tax is finally determined, the portion of the Gross-Up Payment attributable to such reduction plus interest on the amount of such repayment at the applicable federal rate, as defined in Section 1274(b) (2) (B) of the Code. In the event that the Excise Tax is determined to exceed the amount taken into account hereunder at the time of the termination of Employee’s employment (or such other time as is hereinafter described) (including by reason of any payment the existence or amount of which cannot be determined at the time of the Gross-Up Payment), the Company shall make an additional Gross-Up Payment in respect of such excess (plus any interest at the applicable federal rate, penalties or additions payable by Employee with respect to such excess) at the time that the amount of such excess is finally determined. Employee and the Company shall each reasonably cooperate with the other in connection with any administrative or judicial proceedings concerning the existence or amount of liability for Excise Tax with respect to the Total payments.

II. Other Changes

1. Amendment to Section 6(c)
   Section 6 (c) in the Employment Agreement is hereby amended to change the reference in the fifth line from “35 miles” to “50 miles”.

2. Amendment to Section 7(b)(i):
   Section 7(b)(i) is hereby amended to delete it and insert the following in place thereof:

   (i) Employee covenants and agrees that during any period in which Base Salary is continued after termination of this Agreement (or in respect of which Base Salary is paid in a lump sum) or for one year after Employee’s voluntary termination of employment without Good Reason or termination of Employee’s employment for cause, he or she will not, on his or her own behalf or as a partner, officer, director, employee, agent, or consultant of any other person or entity, directly or indirectly, engage or attempt to engage in the business of providing or selling services in the United States that are services offered by Employer at the time of the termination of this Agreement, unless waived in writing by Employer in its sole discretion. Employee recognizes that the above restriction is reasonable and necessary to protect the interest of the Employer and its controller subsidiaries and affiliates.
IN WITNESS WHEREOF, Employer and Employee have executed this Amendment to Employment Agreement as of the date first above written.

Magellan Health Services, Inc.

By

Duly Authorized

Employee
CERTIFICATIONS

I, Steven J. Shulman, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Magellan Health Services, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: July 28, 2006

/s/ STEVEN J. SHULMAN
Steven J. Shulman
Chief Executive Officer
CERTIFICATIONS

I, Mark S. Demilio, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Magellan Health Services, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   (b) Designed such control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with generally accepted accounting principles;
   (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting;

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: July 28, 2006

/s/ MARK S. DEMILIO
Mark S. Demilio
Chief Financial Officer
Certification Required by Rule 13a-14(b) and 18 U.S.C. Section 1350 (as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002)

I, Steven J. Shulman, as Chief Executive Officer of Magellan Health Services, Inc (the “Company”), certify, pursuant to 18 U.S.C. Section 1350 (as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002), that to my knowledge:

(1) the accompanying Quarterly Report on Form 10-Q of the Company for the quarterly period ended June 30, 2006 (the “Report”), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: July 28, 2006

/s/ STEVEN J. SHULMAN

Steven J. Shulman
Chief Executive Officer
Certification Required by Rule 13a-14(b) and 18 U.S.C. Section 1350 (as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002)

I, Mark S. Demilio, as Chief Financial Officer of Magellan Health Services, Inc (the “Company”), certify, pursuant to 18 U.S.C. Section 1350 (as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002), that to my knowledge:

(1) the accompanying Quarterly Report on Form 10-Q of the Company for the quarterly period ended June 30, 2006 (the “Report”), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: July 28, 2006

/s/ MARK S. DEMILIO
Mark S. Demilio
Chief Financial Officer