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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
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FORM 10-K

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

For the fiscal year ended December 31, 1997  
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 NUMBER 1-4034

TOTAL RENAL CARE HOLDINGS, INC.

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

Delaware 51-0354549  
(STATE OR OTHER JURISDICTION OF INCORPORATION (I.R.S. EMPLOYER IDENTIFICATION NO.)  
OR ORGANIZATION)

21250 Hawthorne Boulevard, Suite 800, Torrance, California 90503-5517  
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)  
Registrant's telephone number, including area code: (310) 792-2600

Securities registered pursuant to Section 12(b) of the Act: Common Stock, par  
value \$0.001 per share

Name of each exchange on which registered: New York Stock Exchange

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

Indicate by check mark whether the Registrant (1) has filed all reports  
required to be filed by Section 13 or 15(d) of the Securities Exchange Act of  
1934 during the preceding 12 months (or for such shorter period that the  
Registrant was required to file such reports), and (2) has been subject to  
such filing requirements for the past 90 days. ☒

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

The aggregate market value of the Common Stock of the Registrant held by  
non-affiliates of the Registrant on March 16, 1998, based on the price at  
which the Common Stock was sold as of March 16, 1998, was \$2,833,602,632.

The number of shares of the Registrant's Common Stock outstanding as of  
March 16, 1998 was 80,463,321 shares.

DOCUMENTS INCORPORATED BY REFERENCE

None.

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## PART I

### ITEM 1. BUSINESS.

The following should be read in conjunction with the Registrant's Consolidated Financial Statements and the related notes thereto contained elsewhere in this Form 10-K. This Form 10-K contains forward-looking statements which involve risks and uncertainties. The Registrant's actual results may differ significantly from the results discussed in the forward-looking statements. Unless the context otherwise requires, the term "Company" refers to Total Renal Care Holdings, Inc. ("TRCH") and its subsidiaries, including Renal Treatment Centers, Inc. ("RTC"). When discussing results of operations for periods beginning January 1, 1998 and for the purpose of any general discussion of the Company and any forward-looking statements made regarding the Company's operations and any risks associated therewith, the term "Company" refers to TRCH and its subsidiaries, INCLUDING RTC. When discussing historical results of operations for periods prior to January 1, 1998, the term "Company" refers to TRCH and its subsidiaries, NOT INCLUDING RTC. Unless otherwise indicated, all share and per share data of the Company in this Form 10-K reflect the Company's stock splits effected prior to the date hereof.

The Company is the third largest, and largest independent, provider of high-quality dialysis and related services for patients suffering from chronic kidney failure, also known as end stage renal disease ("ESRD"). As of March 15, 1998, the Company provides dialysis and ancillary services to more than 29,800 patients through a network of 392 outpatient dialysis facilities in 33 states, Washington, D.C., Guam, Puerto Rico, Argentina, Italy and the United Kingdom. In addition, the Company provides inpatient dialysis services at 259 hospitals. On February 27, 1998, TRCH completed its merger with RTC, adding 185 facilities, 13,200 patients and more than 130 inpatient hospital contracts (the "Merger"). The Merger was treated as a pooling of interests for accounting purposes.

The Company has implemented an aggressive, yet disciplined, growth strategy since the management-led buyout of the Company from Tenet Healthcare Corporation (the "August 1994 Transaction," as further described in "Management's Discussion and Analysis of Financial Condition and Results of Operations"). In 1996, the Company added 66 outpatient dialysis facilities, 4,800 patients and 32 inpatient hospital contracts to its network. In 1997, the Company added an additional 63 outpatient dialysis facilities, 5,600 patients and 40 inpatient hospital contracts to its network. As of December 31, 1997, RTC, on a stand-alone basis, had 183 outpatient dialysis facilities and approximately 12,800 patients. From January 1 through March 15, 1998, the Company has added 12 outpatient dialysis facilities and 1,200 patients. The Company also has continued to expand its in-house ancillary services to include vascular access management, a transplant services program, a pediatric renal program and a clinical research organization ("Total Renal Research" or "TRR") in addition to the ESRD laboratory and pharmacy facilities established in 1995. The increase in the number of facilities and hospital contracts, combined with the enhancement of the Company's ancillary businesses and the growth in existing businesses, has resulted in an increase in net operating revenues of 61% to \$438.2 million in the fiscal year ended December 31, 1997 as compared to the prior year and an increase in operating income of 64% to \$79.9 million during the same period.

#### THE DIALYSIS INDUSTRY

##### End-Stage Renal Disease

ESRD is the state of advanced renal impairment that is irreversible and requires routine dialysis treatments or kidney transplantation to sustain life. Qualified patients with ESRD have been entitled, since 1972, to Medicare benefits regardless of age or financial circumstances. According to figures published by the Health Care Financing Administration ("HCFA"), the number of patients requiring chronic dialysis services in the U.S. has increased at a 9% compounded annual growth rate to 200,000 patients in 1995 from 66,000 in 1982. The Company estimates that there are currently 230,000 ESRD patients in the United States and that the United States market for outpatient and inpatient services to ESRD patients in 1997 exceeded \$14 billion.

The Company attributes the continuing growth in the number of ESRD patients principally to the aging of the general population and to better treatment and longer survival of patients with hypertension, diabetes and other illnesses that lead to ESRD. Management also believes improved medical and dialysis technology has enabled older patients and those who previously could not tolerate dialysis due to other illnesses to benefit from this life-prolonging treatment.

The Company estimates there were approximately 3,000 dialysis facilities in the United States at the beginning of 1997, of which approximately 26% were owned by independent physicians (down from 37% in 1992), 25% were hospital-based facilities (down from 33% in 1992), and 49% were owned by five major multi-facility dialysis providers (up from 30% in 1992), including the Company. The dialysis services industry has been undergoing rapid consolidation. The Company believes that many physician owners are selling their facilities to obtain relief from changing government regulation and administrative constraints, to enable them to focus on patient care and to realize a return on their investment. Moreover, the growth of managed care organizations has led owners of private centers to sell to chains, which are better positioned to meet the challenges of managed care. Hospitals are also motivated to sell or outsource management of their facilities as they refocus their resources on their core business due to increasing competitive pressures within the hospital industry. The Company believes that these changes in the health care environment will continue to drive consolidation within the dialysis services industry.

The Company estimates that 72%, or approximately 585,000, of the 815,000 ESRD patients worldwide are located outside the United States. International markets are comprised of highly fragmented delivery systems and several large underserved markets. The Company believes that the compounded annual net patient growth rate internationally is 9-10%.

#### Treatment Options for End-Stage Renal Disease

Treatment options for ESRD include hemodialysis, peritoneal dialysis and kidney transplantation. ESRD patients are treated predominantly in outpatient treatment facilities. HCFA estimates that, during 1996, 85% of the ESRD patients in the United States were receiving hemodialysis treatment in outpatient facilities, with the remaining patients being treated in the home either through peritoneal dialysis (14%) or home hemodialysis (1%).

**Hemodialysis.** Hemodialysis, the most common form of ESRD treatment, is generally performed either in a freestanding facility or in a hospital-based facility. Hemodialysis uses an artificial kidney, called a dialyzer, to remove certain toxins, fluids and salt from the patient's blood, combined with a machine to control external blood flow and to monitor certain vital signs of the patient. The dialysis process occurs across a semi-permeable membrane that divides the dialyzer into two distinct chambers. While blood is circulated through one chamber, a pre-mixed dialyzer fluid is circulated through the other chamber. The toxins and excess fluid from the blood selectively cross the membrane into the dialysis fluid. A hemodialysis treatment usually lasts approximately three hours and is usually performed three times per week per patient.

**Peritoneal Dialysis.** Peritoneal dialysis is generally performed by the patient at home. There are several variations of peritoneal dialysis. The most common are continuous ambulatory peritoneal dialysis ("CAPD") and continuous cycling peritoneal dialysis ("CCPD") or automated peritoneal dialysis ("APD"). All forms of peritoneal dialysis use the patient's peritoneal (abdominal) cavity to eliminate fluid and toxins from the patient. CAPD utilizes a sterile, pharmaceutical-grade dialysis solution which is introduced into the patient's peritoneal cavity through a surgically placed catheter. Toxins in the blood continuously cross the peritoneal membrane into the dialysis solution. After several hours, the patient drains the used dialysis solution and replaces it with fresh solution. CCPD and APD are performed in a manner similar to CAPD, but use a mechanical device to cycle dialysis solution while the patient is sleeping or at rest.

**Other Treatment Options.** An alternative treatment not provided by the Company is kidney transplantation. However, the Company does provide both pre- and post-transplant nursing services and provides transplant pharmaceuticals in selected markets. While transplantation, when successful, is generally the most desirable form of therapeutic intervention, the shortage of suitable donors limits the availability of this treatment option.

## BUSINESS STRATEGY

The Company has implemented an aggressive, yet disciplined, growth strategy since the August 1994 Transaction. In 1996, the Company added 66 outpatient dialysis facilities, 4,800 patients and 32 inpatient hospital contracts to its network. In 1997, the Company added an additional 63 outpatient dialysis facilities, 5,600 patients and 40 inpatient hospital contracts to its network. As of December 31, 1997, RTC, on a stand-alone basis, had 183 facilities and approximately 12,800 patients. From January 1 through March 15, 1998, the Company has added 12 outpatient dialysis facilities, and 1,200 patients. The Company also has continued to expand its in-house ancillary services to include vascular access management, a transplant services program, a pediatric renal program and a clinical research organization in addition to the ESRD laboratory and pharmacy facilities established in 1995. The increase in the number of facilities and hospital contracts, combined with the enhancement of the Company's ancillary businesses and the growth in existing businesses, has resulted in an increase in net operating revenues of 61% to \$438.2 million in the fiscal year ended December 31, 1997 as compared to the prior year and an increase in operating income of 64% to \$79.9 million during the same period. As part of its growth strategy, the Company continually reviews and evaluates potential acquisition candidates and seeks to identify locations for de novo developments. The Company is currently developing approximately 30 new facilities scheduled for completion during 1998.

The Company's growth strategy is focused on establishing strong regional networks of clustered facilities that provide comprehensive care for ESRD patients. The Company believes that this approach enhances its operating efficiency and positions the Company to be a leader in a health care environment increasingly influenced by managed care. The Company strives to continue its growth and margin improvement by (i) expanding its existing networks and by creating new regional facility networks through acquisitions, de novo developments and the formation of hospital alliances, (ii) forming strategic alliances with managed care organizations and physicians, (iii) expanding the range of ancillary services it provides to patients, (iv) continuously improving the quality of care provided through the Company's Quality Management Program and (v) maximizing operating efficiencies and utilization.

### Creation and Expansion of the Facility Networks

**Acquisitions.** The Company's acquisition strategy is to leverage its operating infrastructure in existing regions by acquiring centers where the Company already has a strong market presence and to establish a strong presence in new markets by acquiring clusters of facilities that can support new regional operating infrastructures. In reviewing a potential acquisition, the Company's evaluation includes analyzing financial pro formas, reviewing the local competitive market and assessing the target facility's reputation for providing quality care. In fiscal year 1997, the Company acquired 51 new facilities. From January 1 through March 15, 1998, the Company has acquired 10 facilities. The new facilities acquired subsequent to January 1, 1997 have expanded the Company's existing facility networks in Southern and Northern California, the Minneapolis/St. Paul region and South Florida while providing significant entries into new markets including Detroit, Michigan and New York, New York, as well as North Carolina and Puerto Rico.

**De Novo Developments.** The Company develops new facilities to further enhance its regional clusters, to better serve the managed care market, to accommodate the growing number of ESRD patients and to satisfy demand by local nephrologists. The Company has established an expertise in the design and construction of dialysis facilities, having developed 12 facilities during fiscal year 1997. During 1997, de novo developments enhanced existing regional clusters in Southern and Northern California, South Florida, and Minnesota, as well as El Paso, Texas, Detroit, Michigan and New Orleans, Louisiana.

**Hospital Alliances.** Management believes alliances with hospital-based facilities represent a growth opportunity for the Company as hospitals refocus on their core business due to the changing competitive environment in the hospital industry. These alliances allow the Company to be a value-added partner for hospitals through application of the Company's industry-specific expertise to hospital-based dialysis facilities. Accordingly, the Company is actively pursuing alliances with academic medical centers, as well as community and county hospitals. The Company currently has alliances to work with the following academic institutions to

provide the highest quality care for their ESRD patients: University of Southern California, Louisiana State University, Georgetown University, Harbor-UCLA Medical Center, Hennepin County Medical Center/University of Minnesota and the Rogosin Institute in New York City. These academic affiliations help the Company remain on the leading edge of academic advances in the caring for ESRD patients. The Company has an Academic Advisory Board which meets semi-annually to review leading programs and to discuss ways in which the Company and its community physicians can work together on critical research to improve the well being of the growing ESRD patient population.

#### Alliances with Managed Care and Physicians

Alliances with Managed Care. The Company is committed to forming innovative alliances directly with managed care organizations by providing comprehensive, integrated ESRD services that deliver high-quality care and reduce overall health care costs. In July 1995, the Company was awarded the first long-term ESRD contract to develop and manage a dialysis center for Kaiser Permanente ("Kaiser") in San Diego, California and in March 1996 the 25 station facility was opened. The facility currently cares for approximately 130 Kaiser patients through its innovative integrated ESRD program which is currently being expanded to include two additional de novo facilities in the San Diego market. This contract is also the first "partnership" of its type for Kaiser. Kaiser contracts services for one of the largest dialysis and kidney transplant populations (approximately 3,000 patients in California) in the country.

In August of 1997, the Company signed a five-year agreement with Pioneer Provider Network/MedPartners to provide dialysis services throughout California. In addition to this Primary Preferred Provider Agreement, the Company also signed its first Disease Management Program with Pioneer Provider Network/MedPartners to manage their pre-ESRD, ESRD and transplant patients to improve patient outcomes and to enhance the quality of life of this patient population through advanced disease management techniques. MedPartners has over 1.8 million capitated lives, with over 1.5 million of these lives in Southern California, including approximately 500 ESRD patients.

The Company has also developed innovative programs with payors throughout the country, including Aetna-New Orleans and Maxicare-New Orleans. These payors have selected the Company to be their integrated provider of renal services and have transitioned most of their ESRD patients to the Company's facilities in New Orleans. These payors elected to partner with the Company due to its Quality Management Program, Outcomes Programs and geographic coverage of the regions. As a result of its managed care programs and the Merger, the Company has signed approximately 315 contracts with managed care payors.

Alliances With Physicians. The Company seeks to organize and manage networks of nephrologists which further enhance the ability of these nephrologists and the Company to provide integrated ESRD services. The Company has entered into a long-term management contract with Total Nephrology Care Network Medical Associates (the "Physician Network"), a network of over 35 leading nephrologists in Southern California that works in partnership with the Company to provide high-quality, integrated ESRD services while reducing total costs. The Physician Network markets the services of participating nephrologists to preferred provider organizations, insurance companies, health maintenance organizations and other third-party payors for ESRD services both on a discounted fee-for-service basis and on a prepaid or capitated basis. Through a long-term management services agreement, the Company is responsible for providing billing, information systems and other services to the Physician Network. The Company is paid a management fee for all the services provided by the Company to the Physician Network. The Company is actively developing similar physician networks in most of its major markets, including Chicago, South Florida and Minneapolis.

#### Comprehensive Renal Services

The Company is committed to broadening the range of services it provides to its ESRD patients while adding additional sources of revenue and profits. The Company owns two ESRD laboratories, one in Florida and one in Minnesota, that provide both routine (those included in the Medicare composite rate for dialysis) and non-

routine (those for which an additional fee is charged) laboratory tests for its own and other ESRD patients throughout the United States.

The Company opened a pharmacy in February 1995 that provides a comprehensive prescription oral drug program to patients receiving treatments at the Company's facilities. The pharmacy recently began a transplant program that provides immunosuppressive medications that are required to maintain the viability of a transplant patient's new kidney. The pharmacy also provides intradialytic parenteral nutrition ("IDPN") to patients who require such therapy. The Company's dialysis facilities administer erythropoietin ("EPO") and other injectable drugs to patients upon a physician's prescription.

The Company is the majority owner of an entity which provides vascular access management services to ESRD patients. Clotting of the hemodialysis vascular access, the physical entry point to the circulatory system for the dialysis procedure, is one of the most common causes of hospitalization for ESRD patients. The Company's vascular access management program uses diagnostic and preventive procedures to help keep the access point functioning.

The Company has a pre- and post-kidney transplant services program in which transplant nurses and coordinators train and counsel patients and their families while also assisting in the continuous outcomes monitoring required for this population.

The Company's commitment to improving outcomes, reducing costs and enhancing the quality of life in ESRD patients includes research and development of new products and services. Total Renal Research conducts Phase I through Phase IV clinical trials on devices, drugs and new technologies in the renal and renal-related fields. TRR had been in operation for over seventeen years as the Drug Evaluation Unit and became a subsidiary of the Company in 1997. This clinical research organization has conducted over 200 clinical trials, working with over 50 drug companies and ten device companies, over the last 12 years.

The Company is committed to bringing its quality programs and expertise to a national network of pediatric dialysis centers, and the Company believes that it is currently the only non-hospital based provider of comprehensive services to pediatric ESRD patients.

#### Quality Management Program

The Company believes its reputation for quality care is a significant competitive advantage in attracting patients and physicians and in pursuing growth in the managed care environment. The Company engages in organized and systematic efforts to measure, maintain and improve the quality of services it delivers through its Quality Management Program. In response to current payor demands for cost-effective health care treatments with measurable outcomes, the Company has developed a proprietary PC-based, networked clinical information system that provides managed care organizations with detailed patient outcome reports and critical on-line clinical information. The Company has entered into a strategic alliance with a software company to further the development of H.O.M.E.R. (Health Outcomes Management, Evaluation & Research). This system will provide enhancements to the current clinical information system through its patient-centered, clinical management module and will provide operating efficiencies through its financial module. See "--Operations--Quality Assurance."

#### Maximizing Operating Efficiencies

The Company believes it has adequate capacity within its existing facilities network to accommodate greater patient volume and expects such operating leverage to contribute to increasing margins. In addition, at certain of its facilities, the Company is able to add dialysis stations to meet growing demand. The Company will continue to focus on enhancing operating efficiencies, including staffing, purchasing and financial reporting systems and controls.

The Company recently implemented a Best Demonstrated Practices Program that creates value by identifying ways to improve quality of care and to reduce overall cost at each dialysis facility. Once a facility has demonstrated proficiency with a certain practice, information and operational systems are developed and disseminated throughout the organization by the Regional Quality Management Coordinator, Divisional Vice Presidents and Regional Operations staff. This program is focused on improvements in staffing level efficiency, rationalization of drug and ancillary usage, revenue capture and medical supply utilization.

#### RECENT FACILITY NETWORK EXPANSION AND MERGER WITH RTC

The Company has implemented an aggressive, yet disciplined, growth strategy since the August 1994 Transaction. In 1996, the Company added 66 outpatient dialysis facilities, 4,800 patients and 32 inpatient hospital contracts to its network. In 1997, the Company added an additional 63 outpatient dialysis facilities, 5,600 patients and 40 inpatient hospital contracts to its network. On February 27, 1998, the Company completed its merger with RTC, adding 185 facilities and approximately 13,200 patients.

RTC provides dialysis treatments and ancillary services to patients suffering from chronic kidney failure, primarily in its freestanding outpatient dialysis treatment centers or in the patient's home. At December 31, 1997, RTC operated 183 outpatient dialysis facilities in 24 states, the District of Columbia and Argentina, providing dialysis services to approximately 12,800 patients. In addition, RTC currently provides inpatient acute dialysis services to more than 130 hospitals located in its service areas. RTC has expanded rapidly, primarily through acquisitions, increasing the number of dialysis facilities in its network from 78, as of December 31, 1995 to 183, as of December 31, 1997.

The acquisition of RTC will provide the Company with a platform to accelerate its aggressive, yet disciplined, growth plan domestically and internationally. The Merger solidifies the Company's position as the largest independent provider of dialysis services with a total of 392 facilities serving approximately 29,800 patients worldwide. In the United States, the Company operates 350 facilities serving approximately 27,500 patients. The addition of RTC added 13 new markets to the Company's existing domestic operations and increased its penetration in 11 existing markets. As a result of the Merger, the Company has strong market positions in 11 states: California, Colorado, Florida, Georgia, Kansas, Maryland, Minnesota, North Carolina, Oklahoma, Pennsylvania and Texas. Outside the United States, the Company provides dialysis services to approximately 2,300 patients through 42 facilities in Argentina, Italy and the United Kingdom. The Company estimates that approximately 585,000, or 72%, of the estimated 815,000 ESRD patients worldwide are located outside of the United States.

The Company expects to achieve significant cost savings and synergies from the Merger, including: (i) increased revenue potential resulting from a recent legislative change in Medicare as secondary payor, (ii) enhanced revenue growth through applying the Company's ancillary and value-added services (i.e., lab, pharmacy, etc.) to RTC's patients, (iii) enhanced purchasing efficiencies, (iv) improvements in labor productivity and skill mix, (v) the elimination of duplicative overhead expenses and (vi) improved drug and supply utilization. Many of these cost savings and synergies will be achieved by applying the Company's existing programs to RTC's business. After giving effect to these expected cost savings and synergies resulting from the Merger, the Company expects the Merger to be accretive to its earnings in the fiscal year ending December 31, 1998 and thereafter. The Company believes that additional net cost savings and synergies may be realized in 1998 and beyond. No assurances can be made, however, as to the actual amount and timing of cost savings and synergies, if any, that will be realized. In addition, the Company will incur significant one-time merger related costs in early 1998.

Network Expansion From January 1, 1997 Through March 15, 1998

The following chart lists, by state or country, the number of facilities acquired (or managed) and de novo facilities developed by TRCH and RTC from January 1, 1997 through March 15, 1998:

STATE -----	FACILITIES ACQUIRED	DE NOVO DEVELOPED
CA.....	23	4
TX.....	17	3
NC.....	14	0
PA.....	6	1
MI.....	5	1
MD.....	4	2
FL.....	3	2
MN.....	3	1
NY.....	4	0
NV.....	3	0
VA.....	3	0
KS.....	0	3
WA.....	2	1
Puerto Rico.....	2	0
IL.....	2	0
NJ.....	1	1
GA.....	1	1
DC.....	1	0
AZ.....	0	1
UT.....	0	1
OK.....	0	1
	---	---
Subtotal.....	94	23
COUNTRY -----		
Argentina.....	27	1
Italy.....	4	0
United Kingdom.....	3	0
	---	---
Subtotal.....	34	1
Grand Total.....	128	24
	===	===



## OPERATIONS

### Location, Capacity and Use of Facilities

As of March 15, 1998 the Company operates 392 outpatient dialysis facilities with 6,048 dialysis stations. The Company owns or operates, directly or through wholly-owned subsidiary corporations, 336 of these facilities. Of the remaining facilities, 39 are partially owned by physicians and 17 are partially owned by non-physician minority interests. The Company's facilities range in size from three to 54 dialysis stations. The facilities are located in the following states and countries in the following numbers:

STATE	NO. OF FACILITIES	STATE	NO. OF FACILITIES
-----	-----	-----	-----
CA.....	66	HI.....	4
TX.....	36	IN.....	3
MN.....	27	NV.....	3
FL.....	27	Puerto Rico.....	2
NC.....	19	NM.....	2
PA.....	19	SC.....	2
GA.....	18	Guam.....	2
MD.....	15	UT.....	1
OK.....	15	NE.....	1
VA.....	12	WY.....	1
IL.....	11	WI.....	1
AZ.....	8	OH.....	1
KS.....	8	AL.....	1
LA.....	7	DE.....	1
		---	
MI.....	6	Subtotal.....	350
		COUNTRY	
NJ.....	5	Argentina.....	35
CO.....	5	Italy.....	4
MO.....	5	United Kingdom.....	3
NY.....	4	---	
		Subtotal.....	42
WA.....	4		
		Grand Total.....	392
DC.....	4		===
SD.....	4		

The Company also provides acute inpatient dialysis services to 259 hospitals. System-wide, the Company provides training, supplies and on-call support services to all of its CAPD and CCPD patients.

### Operation of Facilities

The Company's dialysis facilities are designed specifically for outpatient hemodialysis and generally contain, in addition to space for dialysis treatments, a nurses' station, a patient weigh-in area, a supply room, a water treatment space used to purify the water used in hemodialysis treatments, a dialyzer reprocessing room (where, with both the patient's and physician's consent, the patient's dialyzer is sterilized for reuse), staff work areas, offices and a staff lounge and kitchen. Many of the Company's facilities also have a designated area for training patients in home dialysis. Each facility also offers amenities for the patients, such as a color television with headsets at each dialysis station.

In accordance with conditions for participation in the Medicare ESRD program, each facility has a qualified Medical Director. See "Physician Relationships." Each facility also has an Administrator, typically a registered nurse, who supervises the day-to-day operations of the facility and its staff. The staff of each facility typically consists of registered nurses, licensed practical or vocational nurses, patient care technicians, a social worker, a registered dietitian, a unit clerk and bio-medical technicians.

All of the Company's facilities offer high-flux and high-efficiency hemodialysis, which most physicians practicing at the Company's facilities deem suitable for most of their patients. High-flux and high-efficiency hemodialysis utilize machinery that allow patients to dialyze in a shorter period of time per treatment because such methods cleanse the blood at a faster rate than conventional hemodialysis. Many of the Company's facilities also offer conventional hemodialysis. The Company considers the equipment installed in its facilities to be among the most technologically advanced equipment presently available to the dialysis industry.

Many of the Company's facilities also offer various forms of home dialysis, primarily CAPD and CCPD. Home dialysis services consist of providing equipment and supplies, training, patient monitoring and follow-up assistance to patients who prefer and are able to receive dialysis treatments in their homes. Patients and their families or other patient assistants are trained by a registered nurse to perform either CAPD or CCPD at home. Company training programs for CAPD or CCPD generally encompass two to three weeks.

#### Inpatient Dialysis Services

The Company provides inpatient dialysis services (excluding physician professional services) to 259 hospitals. These services are required in connection with the hospital's inpatient services to its patients, and the Company renders these services for a per-treatment fee individually negotiated with the hospital. In many instances, the Company transports the dialysis equipment and supplies to the hospital when requested and administers the dialysis treatment. Examples of cases in which such inpatient services are required include patients with acute kidney failure resulting from trauma or similar causes, patients in the early stages of ESRD and ESRD patients who require hospitalization for other reasons.

#### Ancillary Services

Dialysis facilities provide a comprehensive range of ancillary services to ESRD patients, the most significant of which is the administration of pharmaceuticals (including EPO, calcium and iron supplements) upon a physician's prescription. EPO is a bio-engineered protein which stimulates the production of red blood cells and is used in connection with all forms of dialysis to treat anemia, a medical complication frequently experienced by ESRD patients. The Company also has a licensed pharmacy which provides ESRD patients with oral medications and IDPN services upon a physician's prescription. Other ancillary services include studies to test the degree of bone deterioration, electrocardiograms ("EKGs"), nerve conduction studies to test the degree of deterioration of nerves, doppler flow testing to test the effectiveness of the patient's vascular access for dialysis and blood transfusions.

The Company owns two licensed clinical laboratories, located in Florida and Minnesota, specializing in ESRD patient testing. These ESRD laboratories provide various forms of laboratory tests, a large majority of which are performed for the Company's outpatient dialysis facilities. The types of laboratory tests performed at the ESRD laboratories consist of (i) blood tests to manage the ESRD condition, some of the costs of which are reimbursed as part of the dialysis composite rate, (ii) blood tests ordered for co-morbid ESRD conditions (i.e., diseases that are the result of or cause of ESRD) and (iii) general symptom testing. In addition, the Minnesota laboratory provides certain highly-specialized tests, including therapeutic drug monitoring, bone deterioration and renal stone disease monitoring and certain pre- and post-kidney transplant testing.

The Company is the majority owner of an entity which provides vascular access management services to ESRD patients. Clotting of the hemodialysis vascular access, the physical entry point to the circulatory system for the dialysis procedure, is one of the most common causes of hospitalization for ESRD patients. The Company's vascular access management program uses diagnostic and preventive procedures to help keep the access point functioning.

The Company has a pre- and post-kidney transplant services program in which transplant nurses and coordinators train and counsel patients and their families while also assisting in the continuous outcomes monitoring required for this population.

The Company's commitment to improving outcomes, reducing costs and enhancing the quality of life in ESRD patients includes research and development of new products and services. Total Renal Research conducts Phase I through Phase IV clinical trials on devices, drugs and new technologies in the renal and renal-related fields. TRR had been in operation for over seventeen years as the Drug Evaluation Unit and became a subsidiary of the Company in 1997. This clinical research organization has conducted over 200 clinical trials, working with over 50 drug companies and ten device companies, over the last 12 years.

The Company is committed to bringing its quality programs and expertise to a national network of pediatric dialysis centers, and the Company believes that it is currently the only non-hospital based provider of comprehensive services to pediatric ESRD patients.

#### Physician Relationships

A key factor in the success of a dialysis facility is its relationship with local nephrologists. An ESRD patient generally seeks treatment at a facility near such patient's home and where such patient's nephrologist has practice privileges. Consequently, the Company relies on its ability to meet the needs of referring physicians in order to continue to receive physician referrals of ESRD patients.

The conditions of participation in the Medicare ESRD program mandate that treatment at a dialysis facility be "under the general supervision of a Director who is a physician." The Company has engaged qualified physicians or groups of qualified physicians to serve as Medical Directors for each of its facilities. Generally, the Medical Director must be board eligible or board certified in internal medicine or nephrology and have had at least 12 months of experience or training in the care of patients at ESRD facilities. At some facilities, the Company also contracts with one or more physicians to serve as Assistant or Associate Medical Directors or to direct specific programs, such as CAPD training.

Medical Directors, Associate Medical Directors and Assistant Medical Directors enter into written contracts with the Company which specify their duties and establish their compensation (which is fixed for periods of one year or more). Such agreements are generally terminable by either party with advance written notice. The Company believes that this allows the Company to evaluate frequently the quality of the Medical Director's performance; however, the lack of long-term contracts with physicians could result in the loss of certain key physicians at particular facilities, which could have a material adverse effect on the operations of such facilities. The compensation of the Medical Directors and other physicians under contract is separately negotiated for each facility and generally depends upon competitive factors in the local market, the physician's professional qualifications and responsibilities and the size and utilization of the facility or relevant program.

As is often true in the dialysis industry, one or a few physicians account for all or a significant portion of a dialysis facility's patient referral base. Therefore, the Company's selection of a location for a dialysis facility is determined in part by the physician or nephrologist selected (in advance) to serve as the Company's Medical Director. The loss of an important referring physician at a particular facility could have a material adverse effect on the operations of that facility.

Generally, the Company has non-competition agreements with its Medical Directors or referring physicians. In all cases in which the Company acquired a facility from one or more physicians, or where one or more physicians own interests in facilities as partners, members of a limited liability corporation or co-shareholders with the Company, such physicians have agreed to refrain from owning interests in competing facilities within a defined geographic area for various periods. In other cases, physicians who provide Medical Director services have executed non-competition agreements. While not frequent, the Company has from time to time experienced competition from a dialysis facility established by a former Medical Director following the termination of his or her relationship with the Company.

#### Quality Assurance

Quality Management Program. The Company engages in organized and systematic efforts to measure, maintain and improve the quality of services it delivers and believes that it has earned a favorable reputation for

quality in the dialysis community. The Company has implemented a Quality Management Program designed to measure outcomes and improve the quality of its services. The Company also has developed a proprietary PC-based Clinical Information System to support its Quality Management, Outcomes Monitoring, Measurement and Management and Managed Care Programs. The Company's Quality Management Program and Clinical Information System have been developed under the direction of the Company's Vice President, Quality Management and Chief Medical Officer, who is a Clinical Professor of Medicine at the University of California Medical Center in San Francisco. The implementation of the Quality Management Program is being coordinated by the Company's Corporate Director of Quality Management and 26 regional Quality Management Coordinators. The Company has also added a new position, Corporate Director of Integrated Quality Development, overseeing specific areas that impact quality such as Education and Training and Infection Control, adding another dimension to the Company's integrated approach to quality. This corporate quality management team works with each facility's multi-disciplinary quality management team (including the Medical Director) to implement the Program. The Quality Management Program involves all areas of the Company's services, monitoring and evaluating all of the Company's activities with a focus on continuous improvement. These objectives are accomplished through measurable trend analysis based on specific statistical tools for analysis and communication, and through continuing employee and patient education. The Company also compiles patient hospitalization and related patient treatment outcomes data and is developing standards to evaluate such data as part of the Company's national Quality Management Program.

Clinical Information Systems. To support the Quality Management Program and in response to current payor demands for cost-effective health care treatments with measurable outcomes, the Company has developed a proprietary PC-based, networked Clinical Information System that provides facilities and managed care organizations with detailed patient outcome reports and critical clinical information. The Clinical Information System has been rolled-out to most of the Company's facilities (excluding the former RTC facilities). Furthermore, the Company has implemented connectivity between Kaiser's mainframe and the Company's Clinical Information System at the Mission Dialysis Center in San Diego.

H.O.M.E.R. The Company has entered into a strategic alliance with a software company to further the development of H.O.M.E.R. (Health Outcomes Management, Evaluation & Research). This system will provide enhancements to the current clinical information system through its patient-centered, clinical management module and will provide operating efficiencies through its financial module.

Best Demonstrated Practices. The Company recently implemented a Best Demonstrated Practices Program that creates value by identifying ways to improve quality of care and to reduce overall cost at each dialysis facility. Once a facility has demonstrated proficiency with a certain practice, information and operational systems are developed and disseminated throughout the organization by the Regional Quality Management Coordinator and Regional Operations Directors. This program has been focused on improvements in staffing level efficiency, rationalization of drug and ancillary usage, revenue capture and medical supply utilization. The Best Demonstrated Practices Program is being expanded to include all former RTC facilities.

Physicians Advisory Board. The Company has a Physicians Advisory Board consisting of Medical Directors of facilities from different regions of the country who advise management on the Company's Quality Management Program. Members of the Physicians Advisory Board respond to specific questions on quality issues and the Physicians Advisory Board meets semi-annually to discuss Company quality and related operational issues. The Company believes its reputation for quality care is a competitive advantage in attracting new patients and new referring physicians.

Patient Satisfaction. Since 1991, the Company has retained an independent consulting firm to conduct annual patient satisfaction surveys. These surveys track and identify trends in resulting patient satisfaction indicators that are in turn shared with management, Medical Directors and patients for discussion. The Company recently has decided to provide twice-yearly surveys, with rapid feedback to the facilities, in order to enhance this vital area of its Quality Management Program.

## Sources of Revenue Reimbursement

The following table provides information for the periods indicated regarding the percentage of Company net operating revenues provided by (i) the Medicare ESRD program, (ii) Medicaid, (iii) private/alternative payors, such as private insurance and private funds, and (iv) hospital inpatient dialysis services.

	YEAR ENDED MAY 31,	SEVEN MONTHS ENDED DECEMBER 31,		YEARS ENDED DECEMBER 31,		
	----- 1995	1994	1995	1995	1996	1997
Medicare.....	62.0%	59.4%	60.2%	61.8%	61.1%	58.5%
Medicaid.....	8.1	9.3	6.7	6.7	6.1	6.6
Private/alternative payors.....	24.3	26.3	27.9	25.9	27.3	30.0
Hospital inpatient dialysis services.....	5.6	5.0	5.2	5.6	5.5	4.9
	-----	-----	-----	-----	-----	-----
Total.....	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
	=====	=====	=====	=====	=====	=====

Under the Medicare ESRD program, Medicare reimburses dialysis providers for the treatment of individuals who are diagnosed to have ESRD and are eligible for participation in the Medicare program, regardless of age or financial circumstances. For each treatment, Medicare pays 80% of the amount set by the Medicare prospective reimbursement system, and a secondary payor (usually Medicare supplemental insurance or the state Medicaid program) pays approximately 20% of the amount set by the Medicare prospective reimbursement system. All of the states in which the Company operates dialysis facilities provide Medicaid benefits to qualified recipients to supplement their Medicare entitlement. The Medicare and Medicaid programs are subject to statutory and regulatory changes, administrative rulings, interpretations of policy and governmental funding restrictions, some of which may have the effect of decreasing program payments, increasing costs or modifying the way the Company operates its dialysis business. See "--Medicare Reimbursement."

Assuming a patient is eligible for participation in the Medicare program, the commencement date of Medicare benefits for ESRD patients electing hemodialysis is dependent on several factors. For ESRD patients 65 years of age or older who are not covered by an employer group health plan, Medicare coverage commences immediately. For ESRD patients 65 years of age or older who are covered by an employer group health plan, Medicare coverage commences after a 30-month coordination period. ESRD patients under 65 years of age who are not covered by an employer group health plan (for example, the uninsured, those covered by Medicaid and those covered by an individual health insurance policy) must wait 90 days after commencing dialysis treatments to be eligible for Medicare benefits. During the first 90 days of treatment, the patient, Medicaid or the private insurer is responsible for payment (and, in the case of the individual covered by private insurance, such responsibility is limited to the terms of the policy, with the patient being responsible for the balance). ESRD patients under 65 years of age who are covered by an employer group health plan must wait 33 months after commencing dialysis treatments before Medicare becomes the primary payor. During the first 33 months of treatments, the employer group health plan is responsible for payment at its negotiated rate or, in the absence of such a rate, at the Company's usual and customary rates, and the patient is responsible for deductibles and co-payments, if applicable, under the terms of the employer group health plan.

If an ESRD patient with an employer group health plan elects home dialysis training during the first 90 days of dialysis, Medicare becomes the primary payor after 30 months. If an ESRD patient without an employer group health plan begins home dialysis training during the first three months of dialysis, Medicare immediately becomes the primary payor.

On August 10, 1993, the provisions of the Omnibus Budget Reconciliation Act of 1993 ("OBRA 93") became effective. The OBRA 93 provisions were originally interpreted by HCFA to require employer group health sponsored insurance plans ("EGHP") to be the primary payor for ESRD patients for the first 18 months of service regardless of whether such patients were otherwise Medicare eligible. In April 1995, HCFA issued instructions of clarification to the fiscal intermediaries that Medicare would continue as the primary payor during such period if such patients were originally Medicare eligible but not yet suffering from ESRD. In January 1998, a permanent injunction was issued by a federal court preventing HCFA from retroactively applying its

reinterpretation of the OBRA 93 regulations as unlawful retroactive rule-making. Accordingly, the Company has recognized as revenue payments from private payors in excess of the revenue previously recognized at lower rates which are attributable to such patients.

#### Certain Payor Arrangements

The Company has entered into contracts with third-party payors, including many leading health maintenance organizations in the Company's service areas, to provide dialysis services to their beneficiaries. The Company is a party to non-exclusive agreements with certain of such third-party payors and termination of such third-party agreements could have an adverse effect on the Company. The Company has a contract with the Department of Health and Human Services Navajo Area Indian Health Service to provide (i) chronic dialysis services to Native Americans at the Company's facilities in Farmington and Shiprock, New Mexico as well as at the Company's facilities in Chinle, Kayenta, Tuba City and Ganado, Arizona and (ii) acute dialysis in Indian Health Service Hospitals in Chinle and Tuba City (the "Indian Health Service Contract"). The Company is providing dialysis services to a substantial number of chronic dialysis patients pursuant to the Indian Health Service Contract.

#### Medicare Reimbursement

The Company is reimbursed by Medicare under a prospective reimbursement system for chronic dialysis services provided to ESRD patients. Under this system, the reimbursement rates are fixed in advance and have been adjusted from time to time by Congress. Although this form of reimbursement limits the allowable charge per treatment, it provides the Company with predictable and recurring per treatment revenues and allows the Company to retain any profit earned. Medicare has established a composite rate set by HCFA that governs the Medicare reimbursement available for a designated group of dialysis services, including the dialysis treatment, supplies used for such treatment, certain laboratory tests and certain medications. The Medicare composite rate is subject to regional differences based upon certain factors, including regional differences in wage earnings. Certain other services and items are eligible for separate reimbursement under Medicare and are not part of the composite rate, including certain drugs (including EPO), blood (for amounts in excess of three units per patient per year), and certain physician-ordered tests provided to dialysis patients. Claims for Medicare reimbursement must generally be presented within 15 to 27 months of treatment depending on the month in which the service was rendered and for Medicaid secondary reimbursement, if applicable, within 60 to 90 days after payment of the Medicare claim. The Company generally submits claims monthly and is usually paid by Medicare within 30 days of submission. If in the future Medicare were to include in its composite reimbursement rate any of the ancillary services presently reimbursed separately, the Company would not be able to seek separate reimbursement for these services and this would adversely affect the Company's results of operations to the extent a corresponding increase were not provided in the Medicare composite rate.

The Company receives reimbursement for outpatient dialysis services provided to Medicare-eligible patients at rates that are currently between \$117 and \$139 per treatment, depending upon regional wage variations. The Medicare reimbursement rate is subject to change by legislation and recommendations by the Medical Payment Assessment Commission ("MEDPAC," formerly PROPAC). The Medicare ESRD reimbursement rate was unchanged from commencement of the program in 1972 until 1983. From 1983 through December 1990 numerous Congressional actions resulted in net reduction of the average reimbursement rate from a fixed fee of \$138 per treatment in 1983 to approximately \$125 per treatment in 1990. Congress increased the ESRD reimbursement rate, effective January 1, 1991, resulting in an average ESRD reimbursement rate of \$126 per treatment. In 1990, Congress required that the Department of Health and Human Services ("HHS") and MEDPAC study dialysis costs and reimbursement and make findings as to the appropriateness of ESRD reimbursement rates. In January 1998, MEDPAC recommended a 2.7% increase be made in the reimbursement rate. However, Congress has not yet acted on this recommendation, is not required to implement this recommendation and could either raise or lower the reimbursement rate. The Company is unable to predict what, if any, future changes may occur in the rate of reimbursement, or, if made, whether any such changes will have a material effect on the Company's revenues and net earnings.

On June 1, 1989, the FDA approved the production and sale of EPO, and HCFA approved Medicare reimbursement for EPO's use by dialysis patients. EPO stimulates the production of red blood cells and is beneficial in the treatment of anemia, with the effect of reducing or eliminating the need for blood transfusions for dialysis patients. Physicians began prescribing EPO for their patients in the Company's dialysis facilities in August 1989.

Since June 1, 1989, the Medicare ESRD program has provided reimbursement for the administration to dialysis patients of EPO. EPO, a bio-engineered protein, is beneficial in the treatment of anemia, a medical complication frequently experienced by dialysis patients. Most of the Company's dialysis patients receive EPO. The Company had revenues from the administration of EPO (the substantial majority of which are reimbursed through Medicare and Medicaid programs) of approximately 20.2% of net patient revenues, in the fiscal year ended December 31, 1997. Therefore, EPO reimbursement significantly affects the Company's net income. Medicare reimbursement for EPO was reduced from \$11 to \$10 per 1,000 units for services rendered after December 31, 1993. The Office of the Inspector General of HHS recently recommended that Medicare reimbursement for EPO be reduced from \$10 to \$9 per 1,000 units and HHS has concurred with this recommendation; however, HHS has not determined whether it will pursue this change through the rulemaking process. The President's fiscal 1999 budget includes this proposed reduction in EPO reimbursement.

In April 1996, HCFA notified providers that reimbursement of EPO administration for a patient with a hematocrit measurement exceeding 36% would be available only if the 90-day rolling hematocrit measurement for such patient was 36.5% or less. If the 90-day rolling average hematocrit measure exceeded 36.5%, reimbursement for EPO administration would be denied, except in very limited instances. In connection with this notification, HCFA instructed its fiscal intermediaries to review the rolling three month hematocrit averages and to ascertain compliance therewith. TRCH's and RTC's single fiscal intermediary enacted such instructions in December and September, 1997, respectively. Subsequently, HCFA notified its fiscal intermediaries that it was changing the foregoing reimbursement policy. Effective for monthly billing periods beginning on or after March 10, 1998, reimbursement will be available when the 90-day rolling average hematocrit measure exceeds 36.5%, with payment based on the lower of the actual dosage billed for the current month or 80% of the prior month's allowable EPO dosage. In addition, in this notice, HCFA reestablished the authorization to make payment for EPO for a month when the patient's hematocrit exceeds 36%, when accompanied by documentation establishing medical necessity. The Company does not expect this change in reimbursement or this medical review to have a material adverse effect on the Company's revenues. No prediction can be made as to whether future rate or reimbursement method changes will be made. Furthermore, EPO is produced by a single manufacturer, and any interruption of supply or product cost increases could adversely affect the Company's operations. Finally, during the period from November 1997 through February 1998, approximately 25% of the Company's Medicare billings for EPO reimbursement were placed into medical review because of TRCH's intermediary's non-compliance with HCFA EPO reporting audit guidelines.

The Company provides certain of its patients with IDPN, a nutritional supplement administered during dialysis to patients suffering from nutritional deficiencies. The Company has historically been reimbursed by the Medicare program for the administration of IDPN therapy. Beginning in 1993, HCFA designated four durable medical equipment regional carriers ("DMERCs") to process reimbursement claims for IDPN therapy. The DMERCs recently established new, more stringent medical policies for reimbursement of IDPN therapy, and many dialysis providers' claims have subsequently been denied or delayed. Where appropriate, the Company has appealed and continues to appeal such denials. In addition, the DMERCs are reportedly reviewing the existing IDPN medical policies. The final outcome of appeals and the anticipated review is uncertain and may ultimately reduce the number of patients eligible to receive reimbursement for IDPN therapy. The Company has continued to provide IDPN therapy to its patients pending clarification of this policy.

#### Medicaid Reimbursement

Medicaid programs are state administered programs partially funded by the federal government. These programs are intended to provide coverage for patients whose income and assets fall below state defined levels

and who are otherwise uninsured. The programs also serve as supplemental insurance programs for the Medicare co-insurance portion and provide certain coverages (e.g., oral medications) that are not covered by Medicare. State regulations generally follow Medicare reimbursement levels and coverages without any co-insurance amounts. Certain states, however, require beneficiaries to pay a monthly share of the cost based upon levels of income or assets. Further, Florida does not provide Medicaid benefits on a primary insurance basis, but does provide benefits as a secondary insurer to Medicare. Within Florida, various governmental subdivision agencies provide insurance coverage for the indigent who are otherwise uninsured. The Company is a licensed ESRD Medicaid provider in all states in which it does business.

## GOVERNMENT REGULATION

### General

The Company's dialysis operations are subject to extensive governmental regulations at the federal, state and local levels. These regulations require the Company to meet various standards relating to, among other things, the management of facilities, personnel, maintenance of proper records, equipment and quality assurance programs. The dialysis facilities are subject to periodic inspection by state agencies and other governmental authorities to determine if the premises, equipment, personnel and patient care meet applicable standards. To receive Medicare reimbursement, the Company's dialysis facilities must be certified by HCFA. All of the Company's dialysis facilities are so certified.

Any loss by the Company of its various federal certifications, its authorization to participate in the Medicare or Medicaid programs or its licenses under the laws of any state or other governmental authority from which a substantial portion of its revenues is derived or a change resulting from health care reform reducing dialysis reimbursement or reducing or eliminating coverage for dialysis services would have a material adverse effect on the Company's business. To date, the Company has not had any difficulty in maintaining its licenses or its Medicare and Medicaid authorizations. The health care services industry will continue to be subject to intense regulation at the federal and state levels, the scope and effect of which cannot be predicted. No assurance can be given that the activities of the Company will not be reviewed and challenged or that health care reform will not result in a material adverse change to the Company.

### Fraud and Abuse

The Company's dialysis operations are subject to the illegal remuneration provisions of the Social Security Act (sometimes referred to as the "anti-kickback" statute) and similar state laws that impose criminal and civil sanctions on persons who solicit, offer, receive or pay any remuneration, whether directly or indirectly, in return for inducing the referral of a patient for treatment or the ordering or purchasing of items or services that are paid for in whole or in part by Medicare, Medicaid or similar state programs. Violations of the federal anti-kickback statute are punishable by criminal penalties, including imprisonment, fines or exclusion of the provider from future participation in the Medicare and Medicaid programs, and civil penalties, including assessments of \$2,000 per improper claim for payment plus twice the amount of such claim and suspension from future participation in Medicare and Medicaid. Some state statutes also include criminal penalties. While the federal statute expressly prohibits transactions that traditionally have had criminal implications, such as kickbacks, rebates or bribes for patient referrals, its language has not been limited to such obviously wrongful transactions. Court decisions state that, under certain circumstances, the statute is also violated when one purpose (as opposed to the "primary" or a "material" purpose) of a payment is to induce referrals.

In July 1991 and in November 1992, the Secretary of HHS published regulations that create exceptions or "safe harbors" for certain business transactions. Transactions that are structured within the safe harbors will be deemed not to violate the federal illegal remuneration statute. For a business arrangement to receive the protection of a relevant safe harbor, each and every element of the safe harbor must be satisfied. Transactions that do not satisfy all elements of a relevant safe harbor do not necessarily violate the illegal remuneration statute, but may be subject to greater scrutiny by enforcement agencies. The Company believes its arrangements with



referring physicians are in material compliance with applicable laws. The Company seeks wherever practicable to structure its various business arrangements to satisfy as many safe harbor elements as possible under the circumstances. Except with respect to the Company's lease arrangements with referring physicians, which the Company believes materially satisfy all the relevant safe harbor requirements, none of the Company's arrangements satisfy all elements of a relevant safe harbor. Although the Company has never been challenged under these statutes and believes it complies in all material respects with these and all other applicable laws and regulations, there can be no assurance that the Company will not be required to change its practices or experience a material adverse effect as a result of any such challenge.

The conditions of participation in the Medicare ESRD program mandate that treatment at a dialysis facility be "under the general supervision of a Director who is a physician." Generally, the Medical Director must be board eligible or board certified in internal medicine or pediatrics and have had at least 12 months of experience or training in the care of patients at ESRD facilities. The Company has by written agreement engaged qualified physicians or groups of qualified physicians to serve as Medical Directors for its facilities. At some facilities the Company also contracts with one or more physicians to serve as Assistant or Associate Medical Directors, or to direct specific programs, such as CAPD training, or to provide Medical Director services for acute dialysis services provided to hospitals. The compensation of the Medical Directors and other physicians under contract is separately negotiated for each facility and generally depends upon competitive factors in the local market, the physician's professional qualifications and responsibilities and the size and utilization of the facility or relevant program. The aggregate compensation of the Medical Directors and other physicians under contract is fixed for periods of one year or more by written agreement. Because in all cases the Company's Medical Directors and the other physicians under contract refer patients to the Company's facilities, the federal anti-kickback statute may apply. The Company believes it is in material compliance with the anti-kickback statute with respect to its arrangements with these physicians under contract. Among the safe harbors promulgated by the Secretary of HHS is one relevant to the Company's arrangements with its Medical Directors and the other physicians under contract. That safe harbor, generally applicable to personal services and management contracts, sets forth six requirements. None of the Company's agreements with its Medical Directors or other physicians under contract satisfy all of these elements. However, the Company believes that, except in cases where a facility is in transition from one Medical Director to another or where the term of an agreement with a physician has expired and a new agreement is in negotiation, the Company's agreements with its Medical Directors and other physicians under contract satisfy five of the six safe harbor requirements.

Certain of the Company's dialysis facilities are owned by partnerships or limited liability companies in which physicians who refer patients to the facilities hold interests. Because these physicians refer patients to these facilities, the anti-kickback statute may apply. The Company believes these business arrangements are in material compliance with the anti-kickback statute. With regard to the anti-kickback statute, there is a relevant safe harbor (the "small entity investment interests" safe harbor) which, although none of these arrangements satisfies all elements of that safe harbor, the Company believes that each of the above-mentioned partnerships and limited liability companies satisfies a majority of the safe harbor's elements.

Certain of the Company's dialysis facilities are leased from entities in which physicians who refer patients to the centers hold interests. In addition, a medical facility at which the Company provides ESRD ancillary services is leased from physicians who refer patients for the provision of such ancillary services. Because of the referral of patients to the facilities by these physicians, the anti-kickback statute may apply. The Secretary of HHS has promulgated a safe harbor relevant to such arrangements, generally applicable to space rentals. The Company believes that these leases are in material compliance with the anti-kickback statute and that the leases satisfy in all material respects each of the elements of the space rental safe harbor.

On July 21, 1994, the Secretary of HHS proposed a rule that the Secretary said "would modify the original set of safe harbor provisions to give greater clarity to the rulemaking's original intent." The proposed rule would, among other things, make changes to the safe harbors on personal services and management contracts, small entity investment interests and space rentals. The Company does not believe that its conclusions with respect to the application of these safe harbors to its current arrangements as set forth above would change if the proposed

rule were adopted in the form proposed. However, the Company cannot predict the outcome of the rulemaking process or whether changes in the safe harbors rule will affect the Company's position with respect to the anti-kickback statute.

Several states in which the Company operates dialysis facilities have enacted statutes prohibiting physicians from holding financial interests in various types of medical facilities to which they refer patients. In certain of these states, including California, Virginia, Georgia, Florida, Maryland, Kansas, Louisiana and Texas, the Company has joint ownership relationships with referring physicians. The Company believes its joint ownership relationships with these physicians are within the exceptions stated in these various state laws.

A California statute makes it unlawful for a physician who has, or a member of whose immediate family has, a financial interest with or in an entity to refer a person to that entity for laboratory, diagnostic nuclear medicine, radiation oncology, physical therapy, physical rehabilitation, psychometric testing, home infusion therapy, or diagnostic imaging goods or services. Under the statute, "financial interest" includes, among other things, any type of ownership interest, debt, loan, lease, compensation, remuneration, discount, rebate, refund, dividend, distribution, subsidy or other form of direct or indirect payment, whether in money or otherwise, between a physician and the entity to which the physician makes a referral for the items described above. The statute also prohibits the entity to which the referral was made from presenting a claim for payment to any payor for a service furnished pursuant to a prohibited referral and prohibits a payor from paying for such a service. Violation of the statute by a physician is a misdemeanor and subjects the physician to civil fines. Violation of the prohibition on submitting a claim in violation of the statute is a public offense, subjecting the offender to a fine of up to \$15,000 for each violation and possible action against licensure. Some of the Company's facilities perform laboratory services incidental to dialysis services pursuant to the orders of referring physicians; certain laboratory services, which are sometimes performed by laboratories independent of the Company for outpatient dialysis patients, are identified as included among the services for which the Company is financially responsible under the composite rate under Medicare and under other payment arrangements. Therefore, although the Company does not believe that the statute is intended to apply to laboratory services that are provided incident to dialysis services, it is possible that the statute could be interpreted to apply to such laboratory services. The statute includes certain exemptions from its prohibitions. However, the California statute includes no explicit exemption for Medical Director services or other services for which the Company contracts with and compensates referring physicians in California or for partnership interests of the type held by the referring physicians in eight of the Company's facilities in California. Thus, if the California statute is interpreted to apply to referring physicians with whom the Company contracts, by law, for Medical Director and similar services and with the referring physicians with whom it is in partnership, the Company would be required to restructure some or all of its relationships with such referring physicians. The consequences of such restructuring, if any, cannot be predicted.

A Virginia statute (the "Virginia Statute") generally prohibits a physician from referring a patient for health services to an entity outside the physician's office if the physician or any of the physician's immediate family members is an investor in such entity unless the physician directly provides health services within the entity and will be personally involved with the provision of care to the referred patient or has been granted an exception by the Virginia Board of Health Professions (the "Virginia Board"). Violation of the Virginia Statute by the physician constitutes grounds for disciplinary action as unprofessional conduct and subjects the entity to which a prohibited referral is made to a monetary penalty of not more than \$20,000 per referral, bill or claim if the entity knows or has reason to know that the referral is prohibited by the Virginia Statute. With respect to investment interests acquired prior to February 1, 1993, compliance with the Virginia Statute was required by July 1, 1996. Investment interests of the physicians holding minority interests in the Company's Virginia facilities were acquired prior to February 1, 1993. The Company believes it is reasonable to argue that physicians who refer patients to dialysis facilities directly provide health care within such facilities and are personally involved with the provision of care to such referred patients within the meaning of the Virginia Statute. However, the Company is unaware of any official interpretation of the Virginia Statute by any agency charged with its enforcement that either supports or rejects this interpretation of the Virginia Statute. The Company also believes that, as a public policy matter, it would be reasonable to argue that the Virginia Board should grant an exception to a physician

who is an investor in a dialysis facility to which such physician refers his or her patients for care. However the Company is not aware of the grant of any exception by the Board with respect to ownership interests in dialysis facilities by physicians who refer patients to such facilities. The Company believes that, if necessary, the ownership of its Virginia facilities could be restructured to conform to the requirements of the Virginia Statute.

A Georgia statute (the "Georgia Statute"), prohibits a health care provider (defined to include physicians) from referring a patient for the provision of designated health services to an entity in which the health care provider has an investment interest, unless the provider satisfies certain disclosure requirements. An "investment interest" is defined as an equity or debt security issued by an entity, including shares of stock in a corporation, units or other interests in a partnership, bonds, debentures, notes or other equity interest or debt instruments, but excludes investments in a publicly held corporation with total assets over \$50 million whose shares are traded on a national exchange or over-the-counter market if the investment interest constitutes ownership of less than one percent of the corporation, there are no special stock classes for health care provider investors, and no income from the investment interest is tied to the volume of referrals. The term "entity" is defined as any individual, partnership, firm, corporation or other business entity. A "designated health service" is defined as clinical laboratory services, physical therapy services, rehabilitation services, diagnostic imaging services, pharmaceutical services and outpatient surgical services. While dialysis is not itself a designated health service, a dialysis supplier could be subject to the Georgia Statute to the extent that the dialysis service involves the provision of clinical laboratory services, pharmaceutical services or outpatient surgical services. To comply with the Georgia Statute, the health care provider must furnish the patient with a written disclosure form approved by the health care provider's respective board of licensure, informing the patient of (i) the existence of the investment interest, (ii) the name and address of each applicable entity in which the referring health care provider is an investor and (iii) the patient's right to obtain the items or services at the location or from the health care provider or supplier of the patient's choice. In addition, the provider must post a copy of the disclosure form in a conspicuous public place in the provider's office. The Georgia Statute applies to any consideration paid as compensation or in any manner which is a product of, or incident to, or in any way related to any membership, proprietary interest or co-ownership with an individual, group or organization to whom patients, clients or customers are referred or to any employer-employee or independent contractor relationship including those that may occur in a limited partnership, profit-sharing arrangement, or other similar arrangement with any licensed person to whom these patients are referred. The health care provider or an entity may not present a claim for payment to any individual, third-party payor, or other entity for services provided pursuant to a prohibited referral. If the health care provider or entity improperly collects any amount, the provider or entity must refund such amount to the payor or individual. Any health care provider or other entity that enters into an arrangement or scheme which the health care provider or entity knows or should know has a principal purpose of assuring referrals by the health care provider to a particular entity is subject to a civil penalty of not more than \$50,000 for each such circumvention, arrangement or scheme. Furthermore, any person who presents or causes to be presented a bill for a claim for services that such person knows or should know is for a service for which payment may not be made under the Georgia Statute is subject to a civil penalty of up to \$15,000 for each such service. The Company believes that all physicians who have an investment interest in the Company and who also refer patients to the Company's dialysis facilities are in compliance with the disclosure requirements of the Georgia statute and will be exempt from such statute.

A Florida statute (the "Florida Statute") prohibits health care providers (defined to include physicians) from referring a patient for the provision of designated health services to an entity in which the health care provider is an investor or has an investment interest. The term "designated health services" means clinical laboratory services, physical therapy services, comprehensive rehabilitative services, diagnostic imaging services and radiation therapy services. "Comprehensive rehabilitative services" includes speech, occupational or physical therapy services on an outpatient or ambulatory basis. The term "referral" includes any referral of a patient by a physician for infusion therapy services to a patient of that physician or a member of that physician's group practice. Further, a health care provider may not refer a patient for the provision of any other health care item or service (i.e., an item or service that is not a "designated health service") to an entity in which the health care provider is an investor unless the entity is a publicly traded corporation whose shares are traded on a national

exchange or on the over-the-counter market with total assets over \$50 million, or certain disclosure requirements are met and (i) no more than 50 percent of the value of the investment interests are held by investors who are in a position to make referrals to the entity, (ii) the terms under which an investment interest is offered to an investor who is in a position to make referrals to the entity are no different from the terms offered to investors who are not in a position to make such referrals, (iii) the terms offered to an investor in a position to make referrals are not related to the previous or expected volume of referrals from that investor to the entity and (iv) there is no requirement that an investor make referrals or be in a position to make referrals to the entity as a condition for becoming or remaining an investor. The Florida Statute carries with it penalties of up to \$15,000 for each service for any person who presents or causes to be presented a bill or claim for services that such person knows or should know is prohibited. Furthermore, any health care provider or other entity that enters into an arrangement or scheme which the physician or entity knows or should know has a principal purpose of assuring referrals by the physician to a particular entity may be subject to a civil penalty of up to \$100,000 for each such arrangement. With respect to disclosure requirements for permissible referrals, a health care provider who makes a permitted referral must provide the patient with a written disclosure form informing the patient of extensive information, including the existence of the investment interest, the names and addresses of at least two alternative sources of such services and the name and address of each applicable entity in which the referring provider is an investor. A violation of the disclosure requirements constitutes a misdemeanor and may be grounds for disciplinary action. The Company believes that all physicians with an investment interest in the Company who also refer patients to the Company's dialysis facilities are in compliance with the disclosure requirements of the Florida statute and continue to be exempt from such statute.

A Maryland statute (the "Maryland Statute") prohibits health care practitioners from referring patients to a health care entity in which the health care practitioner or the health care practitioner's immediate family owns a beneficial interest or has a compensation arrangement. The term "compensation arrangement" does not include an arrangement between a health care entity and a health care practitioner or the immediate family member of a health care practitioner for the provision of any services, as an independent contractor, if the arrangement is for identifiable services, the amount of the remuneration under the arrangement is consistent with the fair market value of the service and is not determined in a manner that takes into account, directly or indirectly, the volume or value of any referrals by the referring health care practitioner; and the compensation is provided in accordance with an agreement that would be commercially reasonable even if no referrals were made to the health care provider. The Company believes that it will be exempt from such statute.

A Kansas statute (the "Kansas Statute") defines unprofessional conduct to include referring a patient to a health care entity for services if the licensee (defined to include a physician) has a significant investment interest in the health care entity, unless the licensee informs the patient in writing of such significant investment interest and that the patient may obtain such services elsewhere. A licensee's license may be revoked, suspended or limited in the event the licensee has committed an act of unprofessional conduct. The Kansas Statute defines "health care entity" to mean any corporation, firm, partnership or other business entity which provides services for diagnosis or treatment of human health conditions and which is owned separately from a referring licensee's principal practice. The Kansas Statute also defines "significant investment interest" to mean ownership of at least 10% of the shares of stock of the corporation which owns or leases the health care entity. The Company believes that all physicians who have a financial interest in the Company and who also refer patients to the Company's dialysis facilities are in compliance with the disclosure requirements of the Kansas Statute.

A Louisiana statute (the "Louisiana Statute") prohibits health care providers (defined to include physicians) from making referrals outside the same group practice as that of the referring health care provider to any other health care provider, licensed health care facility, or provider of health care goods and services, including, but not limited to, providers of clinical laboratory services, diagnostic services, medicinal supplies, and therapeutic services when the referring health care provider has a financial interest served by such referral, unless in advance of any such referral, the referring health care provider discloses to the patient, in writing, the existence of such financial interest. The Louisiana Statute defines "financial interest" to mean a significant ownership or investment interest established through debt, equity, or other means and held by a health care provider or a member of a health care provider's immediate family, or any form of direct or indirect remuneration for referral.

Any health care provider who does not comply with the Louisiana Statute disclosure requirement must refund all sums such health care provider received in payment for the goods and services furnished or rendered without disclosure of the financial interest. Such a refund shall be paid to the individual patient, third-party payor, or other entity who made the payment to the health care provider. The Company believes that all physicians who have a financial interest in the Company and who also refer patients to the Company's dialysis facilities are in compliance with the Louisiana Statute.

There are several New York statutes that relate to self-referrals (the "New York Statutes"). Except as discussed below, a practitioner (defined to include physicians) authorized to order clinical laboratory services, pharmacy services, or x-ray or imaging services, generally may not make a referral for such services to an authorized health care provider where such practitioner or an immediate family member has a financial relationship with the health care provider receiving the referral (the "New York Referral Prohibition"). The New York Statutes provide that a health care provider or a referring practitioner may not present or cause to be presented to any individual or third party payor or other entity a claim, bill, or other demand for payment for clinical laboratory services, pharmacy services or x-ray or imaging services that is prohibited. Under the New York Statutes, a "financial relationship" is defined to mean an ownership interest, investment interest or compensation arrangement.

The New York Statutes do make exceptions to the New York Referral Prohibition for certain types of relationships. Generally, the New York Statutes will permit a practitioner to make a referral to a health care provider in which the practitioner or an immediate family member has a financial interest for clinical laboratory services, pharmacy services, and x-ray or imaging services if (i) it is related to practitioner services personally provided by the referring practitioner or provided by a practitioner in the same group as the referring practitioner, (ii) it is related to in-office ancillary services, (iii) it is related to a health maintenance organization or other type of managed care program, (iv) it is related to inpatient hospital services, (v) it is related to referrals by hospitals of patients for clinical laboratory services, pharmacy services, or x-ray or imaging services to be provided by such hospital, (vi) the financial relationship with the hospital does not relate directly to the services for which the referral was made or (vii) it is determined not to pose a substantial risk of payor or patient abuse.

The New York Statutes also make an exception to the New York Referral Prohibition in the event of an ownership interest or investment interest between the practitioner or an immediate family member with a health care provider, upon proper disclosure being made, if (i) the services provided and the practitioner or the patient are located in a rural area, (ii) the ownership interest or investment interest is based on the ownership in a general hospital itself, and not merely a subdivision thereof or (iii) it is related to services provided by an ambulatory surgical center in connection with a surgical procedure performed by the referring practitioner at the ambulatory surgical center.

In addition to providing the exceptions discussed above, the New York Statutes define ownership interests, investment interests, and compensation arrangements, each of which is a part of the definition of a financial relationship, in such a manner as to exclude certain other types of relationships from the New York Referral Prohibition. The New York Statutes provide that an ownership interest or an investment interest generally does not exist based solely on the ownership of investment securities of a publicly traded company with total assets of over \$100,000,000. Further, the New York Statutes generally define a compensation arrangement to not include (i) payments for the rental or lease of space, (ii) administrative services arrangements between a general hospital and a practitioner or immediate family member, (iii) medical director or medical advisory board services arrangements between a health care provider, other than a general hospital, and a practitioner, (iv) recruitment arrangements, (v) isolated financial transactions, (vi) compensation arrangements between a group practice and a salaried practitioner of the group practice and (vii) such other arrangements that are determined not to pose a substantial risk of payor or patient abuse.

With respect to referrals that are not subject to the New York Referral Prohibition, a practitioner must first disclose to the patient the financial relationship prior to making the referral if the financial relationship is either (i) an ownership or investment interest with the health care provider to which the referral is being made or (ii) a

compensation arrangement with such health care provider that is in excess of fair market value or that is based upon the volume and value of the providers' services (the "New York Disclosure Requirement").

Because dialysis itself is not likely a clinical laboratory service, pharmacy service, or x-ray or imaging service, only the New York Disclosure Requirement would need to be satisfied for those joint ownership relationships the Company maintains with referring physicians. The Company believes that to the extent only the New York Disclosure Requirement is applicable, all physicians who have a financial interest in the Company and who also refer patients to the Company's dialysis facilities are in compliance with the New York Statutes. Notwithstanding the above, the Company's facilities in New York may perform laboratory services incidental to dialysis services pursuant to the orders of the referring physicians thereby making the New York Referral Prohibition applicable. Although the Company does not believe that the New York Referral Prohibition is intended to apply to laboratory services that are provided incident to dialysis services, it is possible that the New York Referral Prohibition could be interpreted to apply to such laboratory services. While the New York Statutes contain a number of exceptions to the New York Referral Prohibition, there is no explicit exception for Medical Director services or other services for which the Company contracts with and compensates referring physicians in New York. Thus, if the New York Statutes are interpreted to apply to referring physicians with whom the Company contracts, the Company could be required to restructure some or all of its relationships with such referring physicians. The consequences of such restructuring, if any, cannot be predicted.

The Company believes it is in material compliance with current applicable laws and regulations. No assurance can be made that in the future the Company's business arrangements, past or present, will not be the subject of an investigation or prosecution by a federal or state governmental authority. Such an investigation or prosecution could result in any, or any combination, of the penalties discussed above depending upon the agency involved in such investigation and prosecution. None of the Company's business arrangements with physicians, vendors, patients or others have been the subject of investigation by any governmental authority. No assurance can be given that the Company's activities will not be reviewed or challenged by regulatory authorities. The Company monitors legislative developments and would seek to restructure a business arrangement if the Company determined that one or more of its business relationships placed it in material noncompliance with such a statute.

#### Stark I

The Omnibus Budget Reconciliation Act of 1989 includes certain provisions ("Stark I") that restrict physician referrals for clinical laboratory services to entities with which a physician or an immediate family member has a "financial relationship." The entity is precluded from claiming payment for such services under the Medicare or Medicaid programs, is liable for the refund of amounts received pursuant to prohibited claims, can receive civil penalties of up to \$15,000 per service and can be excluded from participation in the Medicare and Medicaid programs. Because of its broad language, Stark I may be interpreted by HCFA to apply to the Company's operations. However, regulations interpreting Stark I have created an exception to its applicability for services furnished in a dialysis facility if payment for those services is included in the ESRD composite rate. The Company believes that its compensation arrangements with Medical Directors and other physicians under contract are in material compliance with the provisions of Stark I.

#### Stark II

The Omnibus Budget Reconciliation Act of 1993 includes certain provisions ("Stark II") that restrict physician referrals for certain "designated health services" to entities with which a physician or an immediate family member has a "financial relationship." The entity is prohibited from claiming payment for such services under the Medicare or Medicaid programs, is liable for the refund of amounts received pursuant to prohibited claims, can receive civil penalties of up to \$15,000 per service and can be excluded from participation in the Medicare and Medicaid programs. Comparable provisions applicable to clinical laboratory services became effective in 1992. Stark II provisions which may be relevant to the Company became effective on January 1, 1995.

Because of its broad language, Stark II may be interpreted by HCFA to apply to the Company's operations. Consequently, Stark II may require the Company to restructure certain existing compensation agreements with its Medical Directors and to repurchase or to request the sale of ownership interests in subsidiaries and partnerships held by referring physicians or, in the alternative, to refuse to accept referrals for designated health services from such physicians. The Company believes, but cannot assure, that if Stark II is interpreted to apply to the Company's operations, the Company will be able to bring its financial relationships with referring physicians into material compliance with the provisions of Stark II, including relevant exceptions. If the Company cannot achieve such material compliance, and Stark II is broadly interpreted by HCFA to apply to the Company, such application of Stark II could have a material adverse effect on the Company. A broad interpretation of Stark II to include dialysis services and items provided incident to dialysis services would apply to the Company's competitors as well.

A "financial relationship" under Stark II is defined as an ownership or investment interest in, or a compensation arrangement between, the physician and the entity. The Company has entered into compensation agreements with its Medical Directors and other referring physicians; some Medical Directors either own stock in a Company subsidiary which operates a particular dialysis facility or a partnership or membership interest in a Company dialysis facility; and certain of the Company's dialysis facilities are leased from entities in which physicians who refer patients to the facilities hold interests. Certain of the Medical Directors, as part of their compensation, and certain of the physicians from whom the Company has acquired dialysis facilities, as part of the consideration for such acquisitions, have acquired stock or stock options in the Company. The Company believes that the granting of the stock and stock options is in material compliance with the anti-kickback statute, Stark II and the various state statutes. However, the proposed Stark II regulations could require the Company to restructure such stock and stock option ownership.

Stark II includes certain exceptions. A personal services compensation arrangement is excepted from Stark II prohibitions if (i) the arrangement is set out in writing, signed by the parties, and specifies the services covered by the arrangement, (ii) the arrangement covers all of the services to be provided by the physician (or an immediate family member of such physician) to the entity, (iii) the aggregate services contracted for do not exceed those that are reasonable and necessary for the legitimate business purposes of the arrangement, (iv) the term of the arrangement is for at least one year, (v) the compensation to be paid over the term of the arrangement is set in advance, does not exceed fair market value, and is not determined in a manner that takes into account the volume or value of any referrals or other business generated between the parties, (vi) the services to be performed do not involve the counseling or promotion of a business arrangement or other activity that violates any state or federal law and (vii) the arrangement meets such other requirements that may be imposed pursuant to regulations promulgated by HCFA. The Company believes that its compensation arrangements with Medical Directors and other physicians under contract materially satisfy the personal services exception to the Stark II prohibitions.

Payments made by a lessor to a lessee for the use of premises are excepted from Stark II prohibitions if (i) the lease is set out in writing, signed by the parties, and specifies the premises covered by the lease, (ii) the space rented or leased does not exceed that which is reasonable and necessary for the legitimate business purposes of the lease or rental and is used exclusively by the lessee when being used by the lessee, subject to certain permitted payments for common areas, (iii) the lease provides for a term of rental or lease for at least one year, (iv) the rental charges over the term of the lease are set in advance, are consistent with fair market value, and are not determined in a manner that takes into account the volume or value of any referrals or other business generated between the parties, (v) the lease would be commercially reasonable even if no referrals were made between the parties and (vi) the lease meets such other requirements that may be imposed pursuant to regulations promulgated by HCFA. The Company believes that its leases with referring physicians materially satisfy the lease of premises exception to the Stark II prohibitions. The Stark II exception provisions that are applicable to physician ownership interests in entities to which they make referrals do not encompass the kinds of ownership arrangements that referring physicians own in Company subsidiaries that operate particular dialysis facilities.

For purposes of Stark II, "designated health services" include: clinical laboratory services, radiology and other diagnostic services, durable medical equipment, parenteral and enteral nutrients, equipment and supplies, prosthetics and prosthetic devices, home health services, outpatient prescription drugs, and inpatient and outpatient hospital services. The Company believes that the language and legislative history of Stark II indicate that Congress did not intend to include dialysis services and the services and items provided incident to dialysis services within the Stark II prohibitions. However, the Company's provision of, or arrangement and assumption of financial responsibility for, outpatient prescription drugs, including EPO and IDPN, clinical laboratory services, facility dialysis services and supplies, home dialysis supplies and equipment, and services to hospital inpatients and outpatients under its dialysis services agreements with hospitals, include services and items which could be construed as designated health services within the meaning of Stark II. Although the Company does not bill Medicare or Medicaid for hospital inpatient and outpatient services, the Company's Medical Directors may request or establish a plan of care that includes dialysis services for hospital inpatients and outpatients that may be considered a referral to the Company within the meaning of Stark II.

#### Medicare

Because the Medicare program represents a substantial portion of the federal budget, Congress takes action in almost every legislative session to modify the Medicare program for the purpose of reducing the amounts otherwise payable from the program to health care providers. Legislation or regulations may be enacted in the future that may significantly modify the ESRD program or substantially reduce the amount paid for Company services. Further, statutes or regulations may be adopted which impose additional requirements in order for the Company to be eligible to participate in the federal and state payment programs. Such new legislation or regulations may adversely affect the Company's business operations.

#### Other Regulations

The Company's operations are subject to various state hazardous waste disposal laws. Those laws as currently in effect do not classify most of the waste produced during the provision of dialysis services to be hazardous, although disposal of non-hazardous medical waste is also subject to regulation. Occupational Safety and Health Administration regulations require employers of workers who are occupationally subject to blood or other potentially infectious materials to provide those workers with certain prescribed protections against bloodborne pathogens. These regulatory requirements apply to all health care facilities, including dialysis facilities, and require employers to make a determination as to which employees may be exposed to blood or other potentially infectious materials and to have in effect a written exposure control plan. In addition, employers are required to provide or employ hepatitis B vaccinations, personal protective equipment, infection control training, post-exposure evaluation and follow-up, waste disposal techniques and procedures, and engineering and work practice controls. Employers are also required to comply with certain record-keeping requirements. The Company believes it is in material compliance with the foregoing laws and regulations.

Some states have established certificate of need ("CON") programs regulating the establishment or expansion of health care facilities, including dialysis facilities. The Company believes it is in material compliance with all state CON Laws, as applicable, in which it does business.

Although the Company believes it complies in all material respects with current applicable laws and regulations, the health care service industry will continue to be subject to substantial regulation at the federal and state levels, the scope and effect of which cannot be predicted by the Company. No assurance can be given that the Company's activities will not be reviewed or challenged by regulatory authorities.

#### COMPETITION

The dialysis industry is fragmented and highly competitive, particularly in terms of acquisition of existing dialysis facilities and developing relationships with referring physicians. Competition for qualified physicians to act as Medical Directors is also high. The Company estimates that there were approximately 3,000 dialysis



facilities in the United States at the beginning of 1997, of which approximately 26% were owned by independent physicians (down from 37% in 1992), 25% were hospital-based facilities (down from 33% in 1992) and 49% were owned by five major multi-facility dialysis providers (up from 30% in 1992). There are also a number of health care providers that have entered or may decide to enter the dialysis business. Certain of the Company's competitors have substantially greater financial resources than the Company and may compete with the Company for acquisitions and developments of facilities in markets targeted by the Company. Competition for acquisitions has increased the cost of acquiring existing dialysis facilities. While it occurs infrequently, the Company has experienced competition from the establishment of a facility by a former Medical Director or referring physician.

#### INSURANCE

The Company carries property and general liability insurance, professional liability insurance and other insurance coverage in amounts deemed adequate by management. However, there can be no assurance that any future claims will not exceed applicable insurance coverage. Furthermore, no assurance can be given that malpractice and other liability insurance will be available at a reasonable cost or that the Company will be able to maintain adequate levels of malpractice insurance and other liability insurance in the future. Physicians practicing at the Company's facilities are required to maintain their own malpractice insurance. However, the Company maintains coverage for the activities of its Medical Directors (but not for their individual private medical practices).

#### EMPLOYEES

As of March 15, 1998, the Company had over 8,830 employees, including a professional staff of approximately 5,332 registered nurses and technicians, a corporate and regional staff of approximately 685 employees and a facilities support and maintenance staff of approximately 2,813 employees. Of the Company's employees, approximately 6,675 are full time employees. Medical Directors of the Company's dialysis facilities are not employees of the Company.

#### RISK FACTORS

In evaluating the Company and its business, the stockholders of the Company should carefully consider the following risk factors in addition to the other information contained herein. This Form 10-K contains statements that constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. Such forward-looking statements relate to future events or the future financial performance of the Company and involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among other things, those discussed below, and such factors could cause actual results to differ materially from those indicated by such forward-looking statements. The Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. In light of these risks and uncertainties, there can be no assurance that the forward-looking information contained in this Form 10-K will in fact transpire.

##### Uncertainties in Integrating Business Operations and Achieving Cost Savings

The Merger represents the largest single acquisition which the Company has made to date. The process of integrating RTC's operations presents a significant challenge to the Company's management and may lead to unanticipated costs. There can be no assurance that the Company will be successful in completing this integration. The integration of RTC's operations, and of its accounting, personnel, administrative, legal, information systems and other functions, involves the risk that key employees may leave even when offered continuing employment. Robert L. Mayer, Jr., RTC's Chairman, Chief Executive Officer and President, and Frederick C. Jansen, RTC's Executive Vice President, were expected to and did resign following the Merger as did certain other officers for whom the Merger constituted an event of constructive discharge, including

Ronald H. Rodgers, Jr., RTC's Chief Financial Officer. Except for such officers, substantially all of the personnel responsible for operations have remained with the Company following the Merger, although there can be no assurances that such personnel will not resign at any point in the future or that they can easily be replaced should they resign. The integration of RTC's operation requires the devotion of a significant amount of time by senior executives of the Company, which may detract from the business operations and development of the Company. There can be no assurance that any of the cost savings, operating efficiencies or other synergies expected to result from the Merger will be accomplished as rapidly as currently expected or at all.

#### Dependence on Medicare, Medicaid and Other Sources of Reimbursement

The Company is reimbursed for dialysis services primarily at fixed rates established in advance under the Medicare End Stage Renal Disease program. Under this program, once a patient becomes eligible for Medicare reimbursement, Medicare is responsible for payment of 80% of the composite rates determined by HCFA for dialysis treatments. Since 1972, qualified patients suffering from ESRD have been entitled to Medicare benefits regardless of age or financial circumstances. Approximately 58.5% of the Company's net patient revenues during the fiscal year ended December 31, 1997 were funded by Medicare. Since 1983, numerous Congressional actions have resulted in changes in the Medicare composite reimbursement rate from a national average of \$138 per treatment in 1983 to a low of \$125 per treatment on average in 1986 and to approximately \$126 per treatment on average at present. No prediction can be made as to whether future rate changes will be made. Reductions in composite rates could have a material adverse effect on the Company's revenues and net earnings. Furthermore, increases in operating costs that are subject to inflation, such as labor and supply costs, without a compensating increase in prescribed rates, may adversely affect the Company's earnings in the future. No prediction can be made as to whether certain services, for which the Company is currently separately reimbursed, may in the future be included in the Medicare composite rate.

Since June 1, 1989, the Medicare ESRD program has provided reimbursement for the administration to dialysis patients of EPO. EPO, a bio-engineered protein, is beneficial in the treatment of anemia, a medical complication frequently experienced by dialysis patients. Most of the Company's dialysis patients receive EPO. The Company had revenues from the administration of EPO (the substantial majority of which are reimbursed through Medicare and Medicaid programs) of approximately 20.2% of net patient revenues, in the fiscal year ended December 31, 1997. Therefore, EPO reimbursement significantly affects the Company's net income. Medicare reimbursement for EPO was reduced from \$11 to \$10 per 1,000 units for services rendered after December 31, 1993. The Office of the Inspector General of HHS recently recommended that Medicare reimbursement for EPO be reduced from \$10 to \$9 per 1,000 units and HHS has concurred with this recommendation; however, HHS has not determined whether it will pursue this change through the rulemaking process. The President's fiscal 1999 budget includes this proposed reduction in EPO reimbursement.

In April 1996, HCFA notified providers that reimbursement of EPO administration for a patient with a hematocrit measurement exceeding 36% would be available only if the 90-day rolling hematocrit measurement for such patient was 36.5% or less. If the 90-day rolling average hematocrit measure exceeded 36.5%, reimbursement for EPO administration would be denied, except in very limited instances. In connection with this notification, HCFA instructed its fiscal intermediaries to review the rolling three month hematocrit averages and to ascertain compliance therewith. TRCH's and RTC's single fiscal intermediary enacted such instructions in December and September 1997, respectively. Subsequently, HCFA notified its fiscal intermediaries that it was changing the foregoing reimbursement policy. Effective for monthly billing periods beginning on or after March 10, 1998, reimbursement will be available when the 90-day rolling average hematocrit measure exceeds 36.5%, with payment based on the lower of the actual dosage billed for the current month or 80% of the prior month's allowable EPO dosage. In addition, in this notice, HCFA reestablished the authorization to make payment for EPO for a month when the patient's hematocrit exceeds 36%, when accompanied by documentation establishing medical necessity. The Company does not expect this change in reimbursement or this medical review to have a material adverse effect on the Company's revenues. No prediction can be made as to whether future rate or reimbursement method changes will be made. Furthermore, EPO is produced by a single manufacturer, and any interruption of supply or product cost increases could

adversely affect the Company's operations. Finally, during the period from November 1997 through February 1998, approximately 25% of the Company's Medicare billings for EPO reimbursement were placed into medical review because of TRCH's intermediary's non-compliance with HCFA EPO reporting audit guidelines.

All of the states in which the Company currently operates dialysis facilities provide Medicaid (or comparable) benefits to qualified recipients to supplement their Medicare entitlement. Approximately 6.6% of the Company's net patient revenues during the fiscal year ended December 31, 1997 were funded by Medicaid or comparable state programs. The Medicaid programs are subject to statutory and regulatory changes, administrative rulings, interpretations of policy and governmental funding restrictions, all of which may have the effect of decreasing program payments, increasing costs or modifying the way the Company operates its dialysis business.

Approximately 34.9% of the Company's net patient revenues during the fiscal year ended December 31, 1997 were from sources other than Medicare and Medicaid. These sources include payments from third-party, non-government payors, at rates that generally exceed the Medicare and Medicaid rates, and payments from hospitals with which the Company has contracts for the provision of acute dialysis treatments. Any restriction or reduction of the Company's ability to charge for such services at rates in excess of those paid by Medicare would adversely affect the Company's net operating revenues and net income. The Company is unable to quantify or predict the degree, if any, of the risk of reductions in payments under these various payment plans. The Company is a party to nonexclusive agreements with certain third-party payors and termination of such third-party agreements could have an adverse effect on the Company.

#### Operations Subject to Government Regulation

The Company is subject to extensive regulation by both the federal government and the states in which the Company conducts its business. The Company is subject to the illegal remuneration provisions of the Social Security Act and similar state laws, which impose civil and criminal sanctions on persons who solicit, offer, receive or pay any remuneration, directly or indirectly, for referring a patient for treatment that is paid for in whole or in part by Medicare, Medicaid or similar state programs. The federal government has published regulations that provide exceptions or "safe harbors" for certain business transactions. Transactions that are structured within the safe harbors are deemed not to violate the illegal remuneration provisions. Transactions that do not satisfy all elements of a relevant safe harbor do not necessarily violate the illegal remuneration statute, but may be subject to greater scrutiny by enforcement agencies. Neither the arrangements between the Company and the Medical Directors of its facilities, nor the minority ownership interests of referring physicians in certain of the Company's dialysis facilities meet all of the necessary requirements to obtain full protection afforded by these safe harbors. Although the Company has never been challenged under these statutes and the Company believes it complies in all material respects with these and all other applicable laws and regulations, there can be no assurance that the Company will not be required to change its practices or relationships with its Medical Directors or with referring physicians holding minority ownership interests or that the Company will not experience material adverse effects as a result of any such challenge.

Stark I restricts physician referrals for clinical laboratory services to entities with which a physician or an immediate family member has a "financial relationship." HCFA has published regulations interpreting Stark I. The regulations specifically provide that services furnished in an ESRD facility that are included in the composite billing rate are excluded from the coverage of Stark I. The Company believes that the language and legislative history of Stark I indicate that Congress did not intend to include laboratory services provided incidental to dialysis services within the Stark I prohibition; however, laboratory services not included in the Medicare composite rate could be included within the coverage of Stark I. Violations of Stark I are punishable by civil penalties which may include exclusion or suspension of a provider from future participation in Medicare and Medicaid programs and substantial fines. Due to the breadth of the statutory provisions, it is possible that the Company's practices might be challenged under this law. A broad interpretation of Stark I would apply to many of the Company's competitors as well.

Stark II restricts physician referrals for certain "designated health services" to entities with which a physician or an immediate family member has a "financial relationship." The Company believes that the language and legislative history of Stark II indicate that Congress did not intend to include dialysis services and the services and items provided incident to dialysis services within the Stark II prohibitions; however, certain services, including the provision of, or arrangement and assumption of financial responsibility for, outpatient prescription drugs, including EPO, and clinical laboratory services, could be construed as designated health services within the meaning of Stark II. Violations of Stark II are punishable by civil penalties, which may include exclusion or suspension of the provider from future participation in Medicare and Medicaid programs and substantial fines. Due to the breadth of the statutory provisions and the absence of regulations or court decisions addressing the specific arrangements by which the Company conducts its business, it is possible that the Company's practices might be challenged under these laws. A broad interpretation of Stark II to include dialysis services and items provided incident to dialysis services would apply to the Company's competitors as well.

It is unlawful in California for a physician who has, or a member of whose immediate family has, a financial interest with or in an entity to refer a person to that entity for, among other services, laboratory services. The Company currently operates facilities in California which account for a significant percentage of net operating revenues. Although the Company does not believe that the statute is intended to apply to laboratory services that are provided incident to dialysis services, it is possible that the statute could be interpreted to apply to such laboratory services. If the California statute were so interpreted, the Company would be required to restructure some or all of its relationships with referring physicians who serve as Medical Directors of the Company's facilities and with the physicians who hold minority interests in certain of the Company's facilities. The Company also operates dialysis facilities and provides laboratory services in Alabama, Colorado, Delaware, Florida, Georgia, Hawaii, Illinois, Kansas, Maryland, Michigan, Minnesota, Missouri, Nebraska, Nevada, New Jersey, New York, Oklahoma and Puerto Rico, all of which have so-called "fraud and abuse" statutes which regulate the Company's relationships with physicians.

At present, ESRD patients eligible for California's Medicaid program, MediCal, are reimbursed for their transportation costs relating to ESRD treatments. If this practice is deemed to violate applicable federal or state law, the Company may be forced to halt that practice and the Company cannot predict the effect the foregoing would have on the desire of such patients to use the Company's services.

The Company's licensed clinical laboratories are also subject to extensive federal and state regulation of performance standards, including the provisions of The Clinical Laboratory Improvement Act of 1967 and The Clinical Laboratory Improvement Amendments of 1988 Act, as well as the federal and state regulations described above. One of the Company's laboratory operations is presently the subject of a third-party carrier review. The third-party carrier has requested medical and billing records for certain patients, and the Company has provided the requested records. The third-party carrier has not informed the Company of the reason for or the nature or scope of its review.

A number of proposals for health care reform have been made in recent years, some of which have included radical changes in the health care system. Health care reform could result in material changes in the financing and regulation of the health care business, and the Company is unable to predict the effect of such changes on its future operations. It is uncertain what legislation on health care reform, if any, will ultimately be implemented or whether other changes in the administration or interpretation of governmental health care programs will occur. There can be no assurance that future health care legislation or other changes in the administration or interpretation of governmental health care programs will not have a material adverse effect on the results of operations of the Company.

#### Risks Inherent in Growth Strategy

The Company's business strategy depends in significant part on its ability to acquire or develop additional dialysis facilities. This strategy is dependent on the continued availability of suitable acquisition candidates and

subjects the Company to the risks inherent in assessing the value, strengths and weaknesses of acquisition candidates, the operations of acquired companies and identifying suitable locations for additional facilities. The Company's growth is expected to place significant demands on the Company's financial and management resources. In recent years, acquisition prices and competition for facilities has increased. To the extent the Company is unable to acquire or develop facilities in a cost-effective manner, its ability to expand its business and enhance results of operations would be adversely affected. In addition, although the Company believes it has a demonstrable track record of integrating the operations of acquired companies, the process for integrating acquired operations, particularly for newly acquired regional clusters, presents a significant challenge to the Company's management and may lead to unanticipated costs or a diversion of management's attention from day-to-day operations. There can be no assurance that the Company will be able to continue its growth strategy or that this strategy will ultimately prove successful. A failure to successfully continue its growth strategy could have an adverse effect on the Company's results of operations.

#### Competition

The dialysis industry is fragmented and highly competitive, particularly in terms of acquisitions of existing dialysis facilities and developing relationships with referring physicians. Competition for qualified physicians to act as Medical Directors is also high. Competition for acquisitions has increased the cost of acquiring existing dialysis facilities. The Company has also from time to time experienced competition from referring physicians who have opened their own dialysis facilities. A portion of the Company's business consists of monitoring and providing supplies for ESRD treatments in patients' homes. Certain physicians also provide similar services and, if the number of such physicians were to increase, which is possible under the proposed Stark II regulations, the Company could be adversely affected.

#### Dependence on Key Personnel

The Company is dependent upon the services and management experience of the Company's executive officers, and accordingly has entered into employment agreements with, and provided a variety of equity incentives to, these executives. The Company's continued growth depends upon its ability to attract and retain skilled employees, in particular highly skilled nurses, for whom competition is intense. The Company believes that its future success will also be significantly dependent on its ability to attract and retain qualified physicians to serve as Medical Directors of its dialysis facilities. The Company does not carry key-man life insurance on any of its officers.

#### Dependence on Physician Referrals

The Company's facilities are dependent upon referrals of ESRD patients for treatment by physicians specializing in nephrology and practicing in the communities served by the Company's dialysis facilities. As is generally true in the dialysis industry, at each facility one or a few physicians account for all or a significant portion of the patient referral base. The loss of one or more key referring physicians at a particular facility could have a material adverse effect on the operations of that facility and could adversely affect the Company's overall operations. Referring physicians own minority interests in certain of the Company's dialysis facilities. If such interests are deemed to violate applicable federal or state law, such physicians may be forced to dispose of their ownership interests. The Company cannot predict the effect such dispositions would have on its business. See "--Operations Subject to Government Regulation."

#### Operations Outside the United States

Approximately 7.7% of the Company's patients are serviced by operations outside the United States. The Company's non-United States operations are subject to certain political, economic and other uncertainties not encountered in United States operations, including risks of civil disturbances (or other risks that may limit or disrupt markets), expropriations and general hazards associated with the assertions of national sovereignty over certain areas in which operations are conducted. The Company's operations outside the United States may face

the additional risk of fluctuating currency values, hard currency shortages, controls of currency exchange and difficulty in repatriation of income or capital. No prediction can be made as to what governmental regulations may be enacted in the future that could adversely affect the international dialysis industry.

#### Forward-Looking Statements

Certain statements contained in this Form 10-K, including without limitation statements containing the words "believes," "anticipates," "intends," "expects" and words of similar import, constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company or industry results to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among others, the following: general economic and business conditions, both nationally and in the regions in which the Company operates; industry capacity; demographic changes; existing government regulations and changes in, or the failure to comply with, government regulations; legislative proposals for health care reform; the ability to enter into managed care provider arrangements on acceptable terms; changes in Medicare and Medicaid reimbursement levels; liability and other claims asserted against the Company; competition; dependence on physician referrals; changes in business strategy or development plans; the ability to attract and retain qualified personnel, including physicians; the lack of assurance that the cost savings, growth opportunities and synergies expected from the Merger will be achieved; the lack of assurances as to the future performance of the combined companies; the availability and terms of capital to fund the expansion of the Company's business, including the acquisition of additional facilities; and other factors referenced in this Form 10-K. GIVEN THESE UNCERTAINTIES, INVESTORS ARE CAUTIONED NOT TO PLACE UNDUE RELIANCE ON SUCH FORWARD-LOOKING STATEMENTS.

#### ITEM 2. PROPERTIES.

The Company operates 392 outpatient dialysis facilities, of which 382 are located in premises leased by the Company or its respective general partnerships, limited liability companies or subsidiary corporations, and ten of which are owned by the Company. The Company's leases generally cover periods from five to ten years and typically contain renewal options of five to ten years at the fair rental value at the time of renewal or at rates subject to consumer price index increases since the inception of the lease. The Company's facilities range in size from approximately 500 to 15,900 square feet, with an approximate average size of 4,900 square feet. The Company's headquarters are located in a 17,000 square foot facility in Torrance, California. The Company's headquarters lease expires in 2008. The Company's general accounting office in Tacoma, Washington, is leased for a term expiring in 2000. The Company maintains a 41,500 square foot facility in Berwyn, Pennsylvania for additional corporate billing and collections purposes. The Berwyn lease expires in 2001. The Company owns an additional property that it is presently leasing to a third party. The Company anticipates acquiring at least three additional properties for use as dialysis facilities during fiscal 1998. The Company considers its physical properties to be in good operating condition and suitable for the purposes for which they are being used.

Certain of the Company's facilities are operating at or near capacity. However, the Company believes it has adequate capacity within most of its existing facilities to accommodate significantly greater patient volume through increased hours and/or days of operation, or through the addition of dialysis stations at a given facility upon obtaining appropriate governmental approvals. With respect to other facilities, the Company believes that it can lease space at economically reasonable rates in the area of each of these facilities. Expansion or relocation of Company facilities would be subject to review for compliance with conditions relating to participation in the Medicare ESRD program. In states that require a CON, approval of a Company application would be necessary for expansion.

ITEM 3. LEGAL PROCEEDINGS.

The Company is subject to claims and suits in the ordinary course of business for which the Company believes it will be covered by insurance. The Company does not believe that the ultimate resolution of pending proceedings, whether the underlying claims are covered by insurance or not, will have a material adverse effect on the Company's financial condition, results of operations or cash flows.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

Not applicable.

## PART II

### ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

The Company's Common Stock is traded on the New York Stock Exchange. The following table sets forth, for the periods indicated, the high and low closing prices for the Common Stock as reported by the New York Stock Exchange.

	HIGH	LOW
Fiscal Year Ended December 31, 1996		
1st Quarter.....	\$19.20	\$16.43
2nd Quarter.....	\$27.08	\$19.65
3rd Quarter.....	\$25.35	\$19.50
4th Quarter.....	\$27.68	\$19.35
Fiscal Year Ended December 31, 1997		
1st Quarter.....	\$21.98	\$18.23
2nd Quarter.....	\$24.11	\$16.88
3rd Quarter.....	\$30.08	\$21.83
4th Quarter.....	\$33.44	\$25.06

The closing price of the Common Stock on March 16, 1998 was \$35.69 per share. As of March 16, 1998 there were approximately 963 holders of the Company's Common Stock named as holders of record by The Bank of New York, the Company's registrar and transfer agent. Since the August 1994 Transaction, the Company has not declared or paid cash dividends to its holders of Common Stock and does not anticipate paying any cash dividends in the foreseeable future. The Company is subject to certain restrictions on its ability to pay dividends on the Common Stock under that certain \$800 Million Revolving Credit Agreement, as amended, by and among the Company and the Lenders party thereto, DLJ Capital Funding, Inc., as Syndication Agent, First Union National Bank, as Documentation Agent, The Bank of New York as Administrative Agent, and BNY Capital Markets, Inc. and Donaldson, Lufkin & Jenrette Securities Corporation, as Co-Arrangers and that certain \$250 Million Term Loan Agreement, as amended, by and among the Company and the Lenders party thereto, DLJ Capital Funding, Inc., as Syndication Agent, The Bank of New York, as Administrative Agent and BNY Capital Markets, Inc. and Donaldson, Lufkin & Jenrette Securities Corporation, as Co-Arrangers.

Effective January 1, 1998, the Company purchased all of the assets of Monterey Park Dialysis Center, Inc. As partial consideration for the purchase the Company issued an aggregate of 37,314 unregistered shares of Common Stock to the two shareholders of Monterey Park Dialysis Center, Inc. on that date. Such unregistered shares were exempt from registration under the Securities Act pursuant to Rule 505 and Rule 506 of Regulation D. No underwriter participated in the transaction and the unregistered shares are not convertible or exchangeable into other equity securities of the Company.



# ITEM 6. SELECTED FINANCIAL DATA.

The following table presents selected consolidated financial and operating data of the Company for the periods indicated. The consolidated financial data as of May 31, 1993, 1994 and 1995 and as of December 31, 1995, 1996 and 1997 and for each of the years in the three year period ended May 31, 1995, the seven month period ended December 31, 1995, and the years ended December 31, 1996 and 1997 have been derived from the Company's audited consolidated financial statements. The consolidated financial data for the seven months ended December 31, 1994 and the year ended December 31, 1995 are unaudited and include all adjustments consisting solely of normal recurring adjustments necessary to present fairly the Company's results of operations for the period indicated. The results of operations for the seven month periods ended December 31, 1994 and 1995 are not necessarily indicative of the results which may occur for the full fiscal year. The following financial and operating data should be read in conjunction with "Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Company's Consolidated Financial Statements filed as part of this Report.

	YEARS ENDED MAY 31,			SEVEN MONTHS ENDED DECEMBER 31, (1)		YEAR ENDED DECEMBER 31,		
	1993	1994	1995	1994	1995	1995	1996	1997
<b>INCOME STATEMENT</b>								
<b>DATA:(2)</b>								
Net operating revenues.....	\$71,576	\$80,470	\$98,968	\$53,593	\$89,711	\$134,843	\$272,947	\$438,205
Facility operating expenses.....	49,440	56,828	65,583	36,012	57,406	86,977	183,987	292,495
General and administrative expenses(3).....	5,292	7,457	9,115	4,916	7,645	11,844	19,267	29,832
Provision for doubtful accounts.....	2,050	1,550	2,371	1,363	1,811	2,819	5,496	8,896
Depreciation and amortization.....	3,434	3,752	4,740	2,586	4,383	6,537	15,368	27,124
Total operating expenses.....	60,216	69,587	81,809	44,877	71,245	108,177	224,118	358,347
Operating income.....	11,360	10,883	17,159	8,716	18,466	26,666	48,829	79,858
Interest expense, net..	9	13	7,203	3,300	5,584	9,244	5,175	13,238
Income before income taxes, minority interests and extraordinary item....	11,351	10,870	9,956	5,416	12,882	17,422	43,654	66,620
Income taxes.....	4,129	4,106	3,511	1,933	4,631	6,209	16,351	25,141
Income before minority interests and extraordinary item....	7,222	6,764	6,445	3,483	8,251	11,213	27,303	41,479
Minority interests in income of consolidated subsidiaries.....	775	1,046	1,593	833	1,784	2,544	3,578	4,502
Income before extraordinary item....	\$ 6,447	\$ 5,718	\$ 4,852	\$ 2,650	\$ 6,467(4)	\$ 8,669(4)	\$ 23,725(4)	\$ 36,977
Income per share before extraordinary item(5).....			\$ 0.27	\$ 0.18	\$ 0.23(4)	\$ 0.35(4)	\$ 0.57(4)	\$ 0.83

	YEARS ENDED MAY 31,			SEVEN MONTHS ENDED DECEMBER 31,	YEARS ENDED DECEMBER 31,	
	1993	1994	1995	1995(1)	1996	1997
<b>OPERATING DATA:</b>						
Outpatient facilities (at period end).....	36	37	57	68	134	197
Treatments(6).....	379,397	423,353	481,537	390,806	1,169,023	1,869,854
Hospitals receiving inpatient services (at period end).....	32	28	48	55	87	127
	MAY 31,			DECEMBER 31,		
	1993	1994	1995	1995	1996	1997

(DOLLARS IN THOUSANDS)

BALANCE SHEET DATA:(2)

Working capital.....	\$14,609	\$20,064	\$ 14,971	\$ 54,691	\$ 99,299	\$146,274
Total assets.....	36,003	43,621	77,558	163,998	374,080	695,340
Long-term debt						
(including current						
portion).....	267	198	88,142	55,894	104,616	358,584
Mandatorily redeemable						
Common Stock(7).....			3,990			
Stockholders' equity						
(deficit).....	29,015	34,733	(30,879)(8)	82,804	230,966	273,672

(See Notes on following page)

- - - - -
- (1) In 1995, the Company changed its fiscal year end to December 31 from May 31.
  - (2) The August 1994 Transaction and subsequent acquisitions had a significant impact on the Company's capitalization and equity securities and on the Company's results of operations. Consequently, the Balance Sheet Data as of May 31, 1995 and as of December 31, 1995, 1996 and 1997 and the Income Statement Data for the fiscal year ended May 31, 1995, for the seven months ended December 31, 1995, and the years ended December 31, 1996 and 1997 are not directly comparable to corresponding information as of prior dates and for prior periods, respectively.
  - (3) General and administrative expenses for the fiscal years ended May 31, 1993 and 1994 include overhead allocations by the Company's former parent of \$235,000 and \$1,458,000, respectively. The overhead allocations for the fiscal year ended May 31, 1993 were made using a different methodology than that used in the fiscal year ended May 31, 1994 and the substantial increase in that year reflects this change in methodology rather than a change in the level of services provided. No overhead allocation was made for the period from March 1, 1994 through the closing of the August 1994 Transaction, at which time the Company began to record general and administrative expenses as incurred on a stand-alone basis. General and administrative expenses for the fiscal year ended May 31, 1994 also reflect \$458,000 in expenses relating to a terminated equity offering.
  - (4) In December 1995, the Company recorded an extraordinary loss of \$2,555,000, or \$0.09 per share, net of tax, on the early extinguishment of debt. In July and September 1996, the Company recorded a combined extraordinary loss of \$7,700,000 or \$0.19 per share net of tax, on the early extinguishment of debt. See Note 8 of Notes to Consolidated Financial Statements.
  - (5) See additional income per share information in the Consolidated Statements of Income. No income per share information is presented for the years ended May 31, 1993 and 1994 as the Company was a wholly-owned subsidiary during those periods.
  - (6) Represents dialysis treatments provided in outpatient facilities, at home and in acute care hospitals. Home dialysis treatments are stated in hemodialysis equivalents. Only treatments rendered by the Company after the acquisition of a facility are included.
  - (7) Mandatorily redeemable Common Stock represents shares of Common Stock issued in certain acquisitions subject to put options that terminated upon the completion of the Initial Public Offering.
  - (8) In connection with the August 1994 Transaction, the Company paid a special dividend to Tenet Healthcare Corporation ("Tenet") of \$81.7 million, including \$75.5 million in cash.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following should be read in conjunction with the Company's Consolidated Financial Statements and the related notes thereto contained elsewhere in this Form 10-K.

BACKGROUND

The Company's wholly-owned subsidiary Total Renal Care, Inc., formerly Medical Ambulatory Care, Inc., was organized in 1979 by Tenet (formerly National Medical Enterprises, Inc.), to own and operate Tenet's hospital-based dialysis services as freestanding dialysis facilities and to acquire and develop additional dialysis facilities in Tenet's markets. The Company was organized to facilitate the August 1994 Transaction which consisted of the sale by Tenet of approximately 75% of its ownership interest to DLJ Merchant Banking Partners, L.P. and certain of its affiliates ("DLJMB"), management of the Company and certain holders of debt securities of the Company. In connection with the August 1994 Transaction, the Company, NME Properties Corporation (a wholly-owned subsidiary of Tenet), Tenet and DLJMB entered into a number of agreements relating to, among other things, corporate governance, the provision of certain services to the Company by Tenet, and restrictions on stock transfers.

In the August 1994 Transaction, the Company paid a special dividend of \$81.7 million, including \$75.5 million in cash, to Tenet out of the net proceeds from (i) the issuance of units consisting of \$100 million in principal amount at maturity of 12% Senior Subordinated Discount Notes due 2004 (the "Discount Notes"), which were issued at approximately 70% of par, and 1,000,000 shares of Common Stock and (ii) borrowing under the Company's revolving credit facility with The Bank of New York (the "TRC Credit Facility"). The Company raised additional capital to fund the continuation of its growth strategy through an initial public offering (the "IPO") on October 30, 1995 in which the Company issued and sold 11,500,000 shares of its Common Stock and raised gross proceeds of \$107 million. Concurrent with the IPO, the Company listed its Common Stock on the New York Stock Exchange under the symbol "TRL." Subsequent to the IPO, the Company changed its fiscal year end from May 31 to December 31.

The Company raised additional capital to further fund its growth strategy with two secondary stock offerings in April and October of 1996 which raised gross proceeds to the Company of approximately \$135 million. In October of 1996 the Company increased its credit facility with The Bank of New York from \$130 million to \$400 million (the "Credit Facility"). With the proceeds from the IPO, the April 1996 secondary offering and the Credit Facility, the Company was able to complete the early retirement of the Discount Notes. On October 24, 1997, the Company increased the Credit Facility to an aggregate of \$1,050,000,000 in two bank facilities (the "Credit Facilities").

Following the August 1994 Transaction, the Company implemented a focused strategy to increase net operating revenues per treatment and improve operating income margins. The Company has significantly increased per-treatment revenues through the addition of in-house clinical laboratory services, improved pricing, increased utilization of ancillary services and the addition of in-house pharmacy services. To improve operating income, the Company began a systematic review of the Company's vendor relations leading to the renegotiation of a number of supply contracts and insurance arrangements that reduced operating expenses. In addition, the Company has focused on improving facility operating efficiencies and leveraging corporate and regional management. These improvements have been offset in part by increased amortization of goodwill and other intangible assets relating to the Company's acquisitions (all of which have been accounted for as purchase transactions, except the Merger) and start-up expenses related to de novo developments.

The Company incurred approximately \$70.4 million of indebtedness as a result of the August 1994 Transaction. The related interest expense had a significant impact on the Company's results of operations for the fiscal year ended May 31, 1995, the seven months ended December 31, 1995 and the fiscal year ended December 31, 1996. The Company's results of operations have also been materially affected by the implementation of the Company's growth strategy subsequent to the August 1994 Transaction. Consequently, the results of operations for the year ended May 31, 1995, the seven months ended December 31, 1995 and the fiscal years ended December 31, 1996 and December 31, 1997 are not directly comparable to the results of operations for comparable prior periods.

## NET OPERATING REVENUES

Net operating revenues are derived primarily from four sources: (i) outpatient facility hemodialysis services, (ii) ancillary services, including EPO administration, clinical laboratory services and intravenous and oral pharmaceutical products and services, (iii) home dialysis services and related products and (iv) inpatient hemodialysis services provided to hospitalized patients pursuant to arrangements with hospitals. Additional revenues are derived from the provision of dialysis facility management services to certain subsidiaries and affiliated and unaffiliated dialysis centers. The Company's dialysis and ancillary services are reimbursed primarily under the Medicare ESRD program in accordance with rates established by HCFA. Payments are also provided by other third party payors, generally at rates higher than those reimbursed by Medicare for up to the first 33 months of treatment as mandated by law. Rates paid for services provided to hospitalized patients are negotiated with individual hospitals. For the year ended May 31, 1995, approximately 62% and 8% of the Company's net patient revenues were derived from reimbursement under Medicare and Medicaid, respectively. For the seven months ended December 31, 1995, approximately 60% and 7% of the Company's net patient revenues were derived from reimbursement under Medicare and Medicaid, respectively. For the years ended December 31, 1996 and December 31, 1997, approximately 61% and 59%, respectively, and 6% and 7%, respectively of the Company's net patient revenues were derived from reimbursement under Medicare and Medicaid, respectively. See "Item 1. Business--Operations--Sources of Revenue Reimbursement."

## QUARTERLY RESULTS OF OPERATIONS

The following table sets forth selected unaudited quarterly financial and operating information for each of the last two calendar years:

	QUARTERS ENDED							
	MARCH 31, 1996	JUNE 30, 1996	SEPTEMBER 30, 1996	DECEMBER 31, 1996	MARCH 31, 1997	JUNE 30, 1997	SEPTEMBER 30, 1997	DECEMBER 31, 1997
	(DOLLARS IN THOUSANDS, EXCEPT PER SHARES AND PER TREATMENT DATA)							
Net operating revenues..	\$50,237	\$64,583	\$73,333	\$84,794	\$89,030	\$104,752	\$113,668	\$130,755
Facility operating expenses.....	33,329	43,318	49,474	57,866	59,636	70,371	75,505	86,983
General and administrative expenses.....	3,901	4,800	4,943	5,623	6,204	7,179	7,614	8,835
Operating income.....	9,551	11,556	13,126	14,596	16,041	18,709	20,997	24,111
Income before extraordinary item....	4,276	5,726	6,536	7,187	7,825	8,866	9,870	10,416
Income per share before extraordinary item(1)..	\$ 0.12	\$ 0.13	\$ 0.15	\$ 0.16	\$ 0.18	\$ 0.20	\$ 0.22	\$ 0.23
Outpatient facilities...	108	116	126	134	139	166	174	197
Treatments.....	217,451	274,256	315,580	361,736	375,050	451,664	489,922	553,218
Net operating revenues per treatment.....	\$231.03	\$235.48	\$232.38	\$234.41	\$237.38	\$ 231.92	\$ 232.01	\$ 236.35
Operating income margin.....	19.0%	17.9%	17.9%	17.2%	18.0%	17.9%	18.5%	18.4%

(1) See additional income per share information in Note 16 of Notes to Consolidated Financial Statements.

Utilization of the Company's services is generally not subject to material seasonal fluctuations. The quarterly variations shown above reflect the impact of increasing labor costs and decreasing margins related to the corresponding costs of providing services and amortization of intangibles from acquired facilities partially offset by the effects of the Best Demonstrated Practices Program implemented in the fourth quarter of 1996.

## RESULTS OF OPERATIONS

The following table sets forth for the periods indicated selected information expressed as a percentage of net operating revenues for such periods:

	YEAR ENDED MAY 31, 1995	SEVEN MONTHS ENDED DECEMBER 31, ----- 1994 1995		YEARS ENDED DECEMBER 31, ----- 1995 1996 1997		
Net operating revenues.....	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Facility operating expenses.....	66.3	67.2	64.0	64.5	67.4	66.8
General and administrative expenses.....	9.2	9.2	8.5	8.8	7.1	6.8
Provision for doubtful accounts.....	2.4	2.5	2.0	2.1	2.0	2.0
Depreciation and amortization...	4.8	4.8	4.9	4.8	5.6	6.2
Operating income.....	17.3	16.3	20.6	19.8	17.9	18.2
Interest expense, net of interest income.....	7.3	6.2	6.2	6.9	1.9	3.0
Income taxes.....	3.5	3.6	5.2	4.6	6.0	5.7
Minority interests.....	1.6	1.6	2.0	1.9	1.3	1.0
Income before extraordinary item.....	4.9	4.9	7.2	6.4	8.7	8.4

### YEAR ENDED DECEMBER 31, 1997 COMPARED TO YEAR ENDED DECEMBER 31, 1996

**Net Operating Revenues.** Net operating revenues increased \$165,258,000 to \$438,205,000 for the year ended December 31, 1997 ("Year End 1997") from \$272,947,000 for the year ended December 31, 1996 ("Year End 1996") representing a 60.6% increase. Of this increase \$163,632,000 was due to increased treatments from acquisitions, existing facility growth and from de novo developments. The remainder was due to an increase in net operating revenues per treatment which was \$234.35 in Year End 1997 compared to \$233.48 in Year End 1996. The increase in operating revenues per treatment was due to increased ancillary services utilization and an increase in affiliated and unaffiliated facility management fees.

**Facility Operating Expenses.** Facility operating expenses consist of costs and expenses specifically attributable to the operation of dialysis facilities, including operating and maintenance costs of such facilities, equipment, direct labor, and supply and service costs relating to patient care. Facility operating expenses increased \$108,508,000 to \$292,495,000 in Year End 1997 from \$183,987,000 in Year End 1996 and as a percentage of net operating revenues, facility operating expenses decreased to 66.8% in Year End 1997 from 67.4% in Year End 1996. This decrease is mostly due to improvements in labor and pharmaceutical costs as a percentage of revenues partially offset by an increase in other facility expenses, consisting primarily of rent and Medical Director fees. In December 1996, the Company implemented its best demonstrated practices program which focuses primarily upon costs incurred in labor and supplies.

**General and Administrative Expenses.** General and administrative expenses include headquarters expense and administrative, legal, quality assurance, information systems and centralized accounting support functions. General and administrative expenses increased \$10,565,000 to \$29,832,000 in Year End 1997 from \$19,267,000 in Year End 1996, and as a percentage of net operating revenues, general and administrative expenses declined to 6.8% in Year End 1997 from 7.1% in Year End 1996. This decline as a percentage of net revenue is a result of revenue growth and economies of scale achieved through the leveraging of corporate staff across a higher revenue base.

**Provision for Doubtful Accounts.** The provision for doubtful accounts increased \$3,400,000 to \$8,896,000 in Year End 1997 from \$5,496,000 in Year End 1996. As a percentage of net operating revenues, the provision for doubtful accounts remained the same at 2.0% for both periods.

**Depreciation and Amortization.** Depreciation and amortization increased \$11,756,000 to \$27,124,000 in Year End 1997 from \$15,368,000 in Year End 1996, and as a percentage of net operating revenues, depreciation and amortization increased to 6.2% in Year End 1997 from 5.6% in Year End 1996. This increase was

attributable to increased amortization due to acquisition activity and increased depreciation from new facility leaseholds and routine capital expenditures.

**Operating Income.** Operating income increased \$31,029,000 to \$79,858,000 in Year End 1997 from \$48,829,000 in Year End 1996, and as a percentage of net operating revenues, operating income increased to 18.2% in Year End 1997 from 17.9% in Year End 1996. This increase in operating income as a percent of revenue is primarily due to decreases in facility operating costs and general and administrative partially offset by an increase in depreciation and amortization all as a percentage of net operating revenue.

**Interest Expense.** Interest expense, net of interest income, increased \$8,063,000 to \$13,238,000 in Year End 1997 from \$5,175,000 in Year End 1996, and as a percentage of net operating revenues, interest expense, net of interest income, was 3.0% in Year End 1997 and 1.9% in Year End 1996. Cash interest expense during Year End 1997 was \$15,678,000 and non-cash interest during the same period was \$0 versus \$2,656,000 and \$4,396,000 in Year End 1996, respectively. Non-cash interest expense during Year End 1996 was related to the Company's Discount Notes which were completely retired through an early extinguishment during the third quarter of 1996. The increase in cash interest expense was due primarily to an increase in borrowings made under the TRCH Credit Facility and the Senior Credit Facilities to fund the Company's acquisitions.

**Provision for Income Taxes.** Provision for income taxes increased \$8,790,000 to \$25,141,000 in Year End 1997 from \$16,351,000 in Year End 1996, and the effective income tax rate, after minority interest expense, decreased to 40.5% in Year End 1997 from 40.2% in Year End 1996. The overall decrease in the effective tax rate is due to a reduction in the blended state rates and a reduction in nondeductible amortization as a percentage of total amortization expense.

**Minority Interests.** Minority interests represent the pretax income earned by physicians and non-physicians who directly or indirectly own minority interests in the Company's partnership affiliates and the net income in two of the Company's corporate subsidiaries. Minority interests increased \$924,000 to \$4,502,000 in Year End 1997 from \$3,578,000 in Year End 1996, and as a percentage of net operating revenues, minority interest decreased to 1.0% in Year End 1997 from 1.3% in Year End 1996. This decrease in minority interest as a percentage of net operating revenues is a result of a relative proportionate decrease in the formation of partnership affiliates and subsidiaries as a percentage of total new acquisitions.

#### YEAR ENDED DECEMBER 31, 1996 COMPARED TO YEAR ENDED DECEMBER 31, 1995

**Net Operating Revenues.** Net operating revenues increased \$138,104,000 to \$272,947,000 for Year End 1996 from \$134,843,000 for the year ended December 31, 1995 ("Year End 1995") representing a 102.4% increase. Of this increase \$119,904,000 was due to increased treatments from acquisitions, existing facility growth and from de novo developments. The remainder was due to an increase in net operating revenues per treatment which was \$233.48 in Year End 1996 compared to \$223.44 in Year End 1995. The increase in operating revenues per treatment was due to the addition of TRC's ESRD laboratory in 1995 resulting in a full year of revenue in 1996, an overall increase in average reimbursement rates, increased ancillary services utilization primarily in the administration of EPO, the opening of its oral pharmaceutical and IV therapy program, and an increase in affiliated and unaffiliated facility management fees.

**Facility Operating Expenses.** Facility operating expenses increased \$97,010,000 to \$183,987,000 in Year End 1996 from \$86,977,000 in Year End 1995 and as a percentage of net operating revenues, facility operating expenses increased to 67.4% in Year End 1996 from 64.5% in Year End 1995. In Year End 1996 the increase in facility operating expenses as a percentage of revenue primarily was due to increased labor and benefits partially incurred as a result of utilizing existing employees of the acquired facilities during transition periods after the acquisitions.

**General and Administrative Expenses.** General and administrative expenses increased \$7,423,000 to \$19,267,000 in Year End 1996 from \$11,844,000 in Year End 1995, and as a percentage of net operating revenues, general and administrative expenses declined to 7.1% in Year End 1996 from 8.8% in Year End 1995. This decline as a percentage of net revenue is a result of revenue growth and economies of scale achieved through the leveraging of corporate staff across a higher revenue base.

Provision for Doubtful Accounts. The provision for doubtful accounts increased \$2,677,000 to \$5,496,000 in Year End 1996 from \$2,819,000 in Year End 1995, and as a percentage of net operating revenues, provision for doubtful accounts decreased to 2.0% in Year End 1996 from 2.1% in Year End 1995. The provision for doubtful accounts is influenced by the amount of net operating revenues generated from non-governmental payor sources. The decrease for Year End 1996 reflects a decline in the older aging categories of accounts receivable due to increased collection efforts.

Depreciation and Amortization. Depreciation and amortization increased \$8,831,000 to \$15,368,000 in Year End 1996 from \$6,537,000 in Year End 1995, and as a percentage of net operating revenues, depreciation and amortization increased to 5.6% in Year End 1996 from 4.8% in Year End 1995. This increase was attributable to increased amortization due to acquisition activity and increased depreciation from new facility leaseholds and routine capital expenditures.

Operating Income. Operating income increased \$22,163,000 to \$48,829,000 in Year End 1996 from \$26,666,000 in Year End 1995, and as a percentage of net operating revenues, operating income decreased to 17.9% in Year End 1996 from 19.8% in Year End 1995. This decrease in operating income as a percent of revenue is primarily due to an increase in facility operating expenses and depreciation and amortization partially offset by a decrease in general and administrative expenses as a percentage of net operating revenues.

Interest Expense. Interest expense, net of interest income, decreased \$4,069,000 to \$5,175,000 in Year End 1996 from \$9,244,000 in Year End 1995, and as a percentage of net operating revenues, interest expense, net of interest income, was 1.9% in Year End 1996 and 6.9% in Year End 1995. Cash interest expense during Year End 1996 was \$2,656,000 and non-cash interest during the same period was \$4,396,000 versus \$1,216,000 and \$8,901,000 in Year End 1995, respectively. The decrease in Year End 1996 interest expense, net of interest income, was due primarily to the early extinguishment of a portion of the Discount Notes in December of 1995 and the remainder in the third quarter of the year ended December 31, 1996 (as discussed in "Liquidity and Capital Resources" below), and offset by short term investment income earned on excess proceeds from the public stock offerings in April and October, 1996.

Provision for Income Taxes. Provision for income taxes increased \$10,142,000 to \$16,351,000 in Year End 1996 from \$6,209,000 in Year End 1995, and the effective income tax rate, after minority interest expense, decreased to 40.6% in Year End 1996 from 41.3% in Year End 1995. The overall decrease in the effective tax rate is due to a reduction in the blended state rates and a reduction in nondeductible amortization as a percentage of total amortization expense.

Minority Interests. Minority interests increased \$1,034,000 to \$3,578,000 in Year End 1996 from \$2,544,000 in Year End 1995, and as a percentage of net operating revenues, minority interest decreased to 1.3% in Year End 1996 from 1.9% in Year End 1995. This decrease in minority interest as a percentage of net operating revenues is a result of a relative proportionate decrease in the formation of partnership affiliates and subsidiaries as a percentage of total new acquisitions.

Extraordinary Loss. In December 1995 the Company redeemed 35% of the accreted value of the Discount Notes for a total redemption price of \$31,912,000. In connection with this redemption, the Company recorded an extraordinary loss of \$2,555,000 (net of income tax effect). In July and September 1996, the Company retired all remaining outstanding Notes for a total redemption price of \$68,499,000. In connection with these redemptions, the Company recorded an extraordinary loss of \$7,700,000 (net of income tax effect).

SEVEN MONTHS ENDED DECEMBER 31, 1995 COMPARED TO SEVEN MONTHS ENDED DECEMBER 31, 1994

Net Operating Revenues. Net operating revenues increased \$36,118,000 to \$89,711,000 for the seven months ended December 31, 1995 ("1995 Seven Month Period") from \$53,593,000 for the seven months ended December 31, 1994 ("1994 Seven Month Period") representing a 67.4% increase. Of this increase \$24,411,000 was due to increased treatments from acquisitions, existing facility growth and from de novo developments. The remainder was due to an increase in net operating revenues per treatment which was \$229.55 in the 1995 Seven



Month Period compared to \$199.36 in the 1994 Seven Month Period, and an increase in affiliated and unaffiliated facility management fees. The increase in operating revenues per treatment was due to the addition of an ESRD laboratory, an overall increase in reimbursement rates, increased ancillary services utilization primarily in the administration of EPO and the opening of the Company's oral pharmaceutical and IV therapy program.

**Facility Operating Expenses.** Facility operating expenses increased \$21,394,000 to \$57,406,000 in the 1995 Seven Month Period from \$36,012,000 in the 1994 Seven Month Period and as a percentage of net operating revenues, facility operating expenses declined to 64.0% in the 1995 Seven Month Period from 67.2% in the 1994 Seven Month Period. In the 1995 Seven Month Period the decrease in facility operating expenses as a percentage of revenue was due to substantial reductions achieved in the costs of providing services, including medical and pharmaceutical supplies, and overall labor resource efficiencies.

**General and Administrative Expenses.** General and administrative expenses increased \$2,729,000 to \$7,645,000 in the 1995 Seven Month Period from \$4,916,000 in the 1994 Seven Month Period, and as a percentage of net operating revenues, general and administrative expenses declined to 8.5% in the 1995 Seven Month Period from 9.2% in the 1994 Seven Month Period. This decline as a percentage of net revenue is a result of revenue growth and economies of scale achieved through the leveraging of corporate staff across a higher revenue base.

**Provision for Doubtful Accounts.** The provision for doubtful accounts increased \$448,000 to \$1,811,000 in the 1995 Seven Month Period from \$1,363,000 in the 1994 Seven Month Period, and as a percentage of net operating revenues, provision for doubtful accounts decreased to 2.0% in the 1995 Seven Month Period from 2.5% in the 1994 Seven Month Period. The provision for doubtful accounts is influenced by the amount of net operating revenues generated from non-governmental payor sources. The decrease for the 1995 Seven Month Period reflects better management of accounts receivable, including increased collection efforts, billing accuracy and improved preauthorization procedures with payors.

**Depreciation and Amortization.** Depreciation and amortization increased \$1,797,000 to \$4,383,000 in the 1995 Seven Month Period from \$2,586,000 in the 1994 Seven Month Period, and as a percentage of net operating revenues, depreciation and amortization increased to 4.9% in the 1995 Seven Month Period from 4.8% in the 1994 Seven Month Period. This increase was attributable to increased amortization due to acquisition activity and increased depreciation from new facility leaseholds and routine capital expenditures.

**Operating Income.** Operating income increased \$9,750,000 to \$18,466,000 in the 1995 Seven Month Period from \$8,716,000 in the 1994 Seven Month Period, and as a percentage of net operating revenues, operating income increased to 20.6% in the 1995 Seven Month Period from 16.3% in the 1994 Seven Month Period. This increase in operating income is primarily due to a decrease in facility operating expenses as a percentage of net operating revenues.

**Interest Expense.** Interest expense, net of interest income, increased \$2,284,000 to \$5,584,000 in the 1995 Seven Month Period from \$3,300,000 in the 1994 Seven Month Period, and as a percentage of net operating revenues, interest expense, net of interest income, was 6.2% in the 1995 Seven Month Period and 6.2% in the 1994 Seven Month Period. Cash interest expense during the 1995 Seven Month Period was \$1,063,000 and non-cash interest during the same period was \$5,228,000 versus \$26,000 and \$3,274,000 in the 1994 Seven Month Period, respectively. The increase in the 1995 Seven Month Period cash interest expense was due primarily to increased borrowing under the Credit Facility and the increase in non-cash interest expense was due to the August 11, 1994 issuance of the Discount Notes, which resulted in four and a half months of interest expense recognized in the 1994 Seven Month Period as compared to a full seven months of interest expense recognized in the 1995 Seven Month Period. In addition, interest accrued in the 1995 Seven Month Period on a higher accreted principal amount through December 7, 1995, on which date the Company redeemed 35% of the principal amount of the Discount Notes at maturity. Cash interest initially would have been incurred on the Discount Notes on August 15, 1997.

Provision for Income Taxes. Provision for income taxes increased \$2,698,000 to \$4,631,000 in the 1995 Seven Month Period from \$1,933,000 in the 1994 Seven Month Period, and as a percentage of net operating revenues, provision for income taxes increased to 5.2% in the 1995 Seven Month Period from 3.6% in the 1994 Seven Month Period. The increase was primarily due to the increased profitability of the Company in the 1995 Seven Month Period versus the same period in the prior year.

Minority Interests. Minority interests increased \$951,000 to \$1,784,000 in the 1995 Seven Month Period from \$833,000 in the 1994 Seven Month Period, and as a percentage of net operating revenues, minority interest increased to 2.0% in the 1995 Seven Month Period from 1.6% in the 1994 Seven Month Period. This increase in minority interest as a percentage of revenue is a result of increased profitability at these partnership affiliates and subsidiaries and an increase in the number of company facilities owned by such partnership affiliates.

Extraordinary Loss. On December 7, 1995 the Company redeemed 35% of the accreted value of the Discount Notes at a redemption premium of 111% for a total redemption price of \$31,912,000. In connection with this redemption, the Company recorded an extraordinary loss of \$2,555,000 (net of income tax effect) in December 1995.

#### LIQUIDITY AND CAPITAL RESOURCES

Sources and Uses of Cash. Net cash provided by operating activities of the Company was \$5,788,000, \$18,447,000, \$6,277,000 and \$15,069,000 for Year End 1997, Year End 1996, 1995 Seven Month Period and the fiscal year ended May 31, 1995, respectively. Net cash provided by operating activities consists of the Company's net income, increased by extraordinary items related to the early extinguishment of debt (for the 1995 Seven Month Period and Year End 1996) and non-cash expenses such as depreciation, amortization, accreted interest and the provision for doubtful accounts, and adjusted by changes in components of working capital, primarily accounts receivable. Net cash used in investing activities was \$276,197,000, \$171,546,000, \$35,130,000 and \$26,607,000 for Year End 1997, Year End 1996, 1995 Seven Month Period and the fiscal year ended May 31, 1995, respectively. The Company's principal uses of cash in investing activities have been related to acquisitions, purchases of new equipment and leasehold improvements for the Company's outpatient facilities, as well as the development of new outpatient facilities. Net cash provided by financing activities was \$255,928,000 for Year End 1997 consisting primarily of proceeds from the Company's Credit Facilities: \$142,799,000 for Year End 1996 consisting primarily of net proceeds from two public issuances of common stock and net proceeds from the Credit Facility, offset by amounts paid in connection with the remaining Discount Notes; \$56,988,000 for the 1995 Seven Month Period consisting primarily of net proceeds from the IPO, less amounts paid in connection with the redemption of 35% of the outstanding Discount Notes and net payments of borrowings under the Credit Facility; and \$12,135,000 for the fiscal year ended May 31, 1995, consisting primarily of debt and equity offering proceeds, and borrowings under the Credit Facility, net of cash dividends paid to Tenet.

Expansion. The Company anticipates aggregate capital requirements for purchases of equipment and leasehold improvements for outpatient facilities including the development costs of 30 de novo facilities in the year ending December 31, 1998 will be approximately \$45,000,000, as compared to \$36,878,000 in Year End 1997.

The Company's strategy is to continue to expand its operations both through development of de novo centers and through acquisitions. The development of a typical outpatient facility generally requires \$700,000 to \$1,000,000 for initial construction and equipment and \$200,000 for working capital. Based on the Company's experience, a de novo facility typically achieves operating profitability, before depreciation and amortization, by the 12th to 15th month of operation. However, the period of time for a development facility to break even is dependent on many factors which can vary significantly from facility to facility, and, therefore, the Company's past experience may not be indicative of the performance of future developed facilities.

From January 1, 1998 through March 15, 1998 the Company has paid approximately \$40 million in consideration for acquisitions involving seven agreements to acquire ten additional facilities. Additionally, the Company has entered into letters of intent to acquire additional facilities for approximately \$100 million.

Credit Facilities. On October 24, 1997, the Company expanded its existing \$400 million Credit Facility with an aggregate of \$1,050,000,000 in two bank facilities. The Credit Facilities consist of a seven-year \$800 million revolving credit facility and a ten-year \$250 million term facility. Under the revolving credit facility, up to \$100,000,000 may be used in connection with letters of credit, and up to \$15,000,000 in short-term funds may be borrowed the same day notice is given to the banks under a "Swing Line" facility. Up to \$75,000,000 of the available letters of credit and borrowings under the revolving credit facility may be utilized for foreign financing. In general, borrowings under the Credit Facilities bear interest at one of two floating rates selected by the Company: (i) the Alternate Base Rate (defined as the higher of The Bank of New York's prime rate or the federal funds rate plus 0.5%) or (ii) Adjusted LIBOR (defined as the 30-, 60-, 90- or 180-day London Interbank Offered Rate, adjusted for statutory reserves) plus a margin that ranges from 0.45% to 1.75% depending on the Company's leverage ratio. Swing Line borrowings bear interest at either a rate negotiated by the Company and the banks at the time of borrowing or, if no rate is negotiated and agreed upon, the Alternate Base Rate.

The Credit Facilities contain financial and operating covenants including, among other things, requirements that the Company maintain certain financial ratios and satisfy certain financial tests, and impose limitations on the Company's ability to make capital expenditures, to incur other indebtedness and to pay dividends. As of the date hereof, the Company is in compliance with all such covenants.

On November 25, 1996, the Company entered into a seven year interest rate swap agreement involving the exchange of fixed and floating interest payment obligations without the exchange of the underlying principal amounts. At December 31, 1997 the total notional principal amount of this interest rate swap agreement was \$100,000,000 and the effective interest rate thereon was 7.57%.

On July 24, 1997, the Company entered into a ten-year interest rate swap agreement. At December 31, 1997 the total notional principal amount of this interest rate swap agreement was \$200,000,000 and the effective interest rate thereon was 7.77%.

Stock Split. On September 30, 1998 the Company declared a five-for-three split of its Common Stock in the form of a stock dividend. Stockholders of record on October 7, 1997 received two additional shares of the Company's Common Stock for every three shares owned. The dividend shares were delivered to the record stockholders on October 20, 1997. The Company issued a cash dividend for all fractional shares of approximately \$14,000 which was also paid on October 20, 1997.

Year 2000 Risks. Certain of the Company's older computer software programs identify years with two digits instead of four. This is likely to cause problems because the programs may recognize the year 2000 as the year 1900. Plans are in process to eliminate all Year 2000 software problems. The Company fully expects to complete the necessary conversions by the end of the second quarter of 1999. The Company believes that the cost of modifying those systems that were not already scheduled for replacement for business reasons prior to 2000 is immaterial. Although the Company does not expect Year 2000 to have a material adverse effect on its internal operations, it is possible that Year 2000 problems could have a significant adverse effect on (i) the Company's suppliers and their ability to service the Company and to accurately process payments received and (ii) the ability of certain third party insurance payors and governmental payors, such as Medicare and the individual state Medicaid programs, to accurately process remittances (payments) on patient accounts receivable due to the Company.

The Merger. The Company expects to achieve significant cost savings and synergies from the Merger. After giving effect to these expected cost savings and synergies, the Company expects the Merger to be accretive to its earnings in the fiscal year ending December 31, 1998 and thereafter. The Company believes that additional net cost savings and synergies may be realized in 1998 and beyond. No assurances can be made, however, as to the actual amount and timing of cost savings and synergies, if any, that will be realized. In addition, the Company will incur significant one-time merger related costs in early 1998.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

See the Index included at "Item 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K."

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None.

# PART III

## ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.

### INFORMATION CONCERNING MEMBERS OF THE BOARD OF DIRECTORS

The following table sets forth certain information concerning members of the Board of Directors of the Company as of December 31, 1997:

NAME	AGE	POSITION
Victor M.G. Chaltiel	56	Chairman of the Board, Chief Executive Officer, President and Director
Maris Andersons	60	Director
Peter T. Grauer	52	Director
Regina E. Herzlinger	54	Director
Shaul G. Massry	67	Director

Victor M.G. Chaltiel has been the Chairman, CEO and President of the Company and a Director of the Company since August 1994. Mr. Chaltiel served as President and CEO of Abbey Healthcare Group, Inc. ("Abbey") from November 1993 to February 1994 and prior thereto as Chairman, CEO and President of Total Pharmaceutical Care, Inc. ("TPC") from March 1989 to November 1993, when Abbey completed its acquisition of TPC. From May 1985 to October 1988, Mr. Chaltiel served as President, Chief Operating Officer and a Director of Salick Health Care, Inc., a publicly-held company focusing on the development of outpatient cancer and dialysis treatment centers. Mr. Chaltiel served in a consulting capacity with Salick Health Care, Inc. from October 1988 until he joined TPC. Prior to May 1985, Mr. Chaltiel was associated with Baxter International, Inc. ("Baxter") for 18 years in numerous corporate and divisional management positions, including Corporate Group Vice President with responsibility for the International Group and five domestic divisions with combined revenue in excess of \$1 billion, President of Baxter's Artificial Organs Division, Vice President of its International Division, Area Managing Director for Europe and President of its French operations. While at Baxter, Mr. Chaltiel was instrumental in the development and successful worldwide commercialization of Continuous Ambulatory Peritoneal Dialysis, currently the most common mode of home dialysis.

Maris Andersons has been a Director of the Company since August 1994. Mr. Andersons was a Senior Vice President and Senior Advisor, Corporate Finance, of Tenet Healthcare Corporation ("Tenet") until his retirement in 1997. Mr. Andersons also has held various senior executive offices with Tenet since 1976. Prior to joining Tenet, Mr. Andersons served as a Vice President of Bank of America.

Peter T. Grauer has been a Director of the Company since August 1994. Mr. Grauer has been a Managing Director of DLJ Merchant Banking, Inc. ("DLJMB") since September 1992. From April 1989 to September 1992, he was a Co-Chairman of Grauer & Wheat, Inc., an investment firm specializing in leveraged buyouts. Prior thereto Mr. Grauer was a Senior Vice President of Donaldson, Lufkin & Jenrette Securities Corporation ("DLJ"). Mr. Grauer is a Director of S.D. Warren Holdings Corporation, Doane Products Co. and Jitney Jungle Stores Co.

Regina E. Herzlinger has been a director of the Company since July 1997. Ms. Herzlinger, the Nancy R. McPherson Professor of Business Administration Chair at the Harvard Business School, has been a member of the faculty at the Harvard Business School since 1971. Ms. Herzlinger is a director of C.R. Bard, Inc., Cardinal Health, Inc., Deere & Company, Manor Care, Inc. and Schering-Plough Corporation.

Shaul G. Massry has been a director of the Company since April 1997. Dr. Massry has been a Professor of Medicine, Physiology and Biophysics and Chief, Division of Nephrology, at the University of Southern California School of Medicine since 1974. Dr. Massry served as the president of the National Kidney Foundation from 1990 through 1992.

No arrangement or understanding exists between any director and any other person or persons pursuant to which any director was or is to be selected as a director other than pursuant to the Shareholders Agreement. See "Item 13. Certain Relationships and Related Transactions." None of the directors has any family relationship among themselves or with any executive officer of the Company.

#### INFORMATION CONCERNING EXECUTIVE OFFICERS

The following table sets forth certain information concerning each person who is an executive officer of the Company as of December 31, 1997:

NAME	AGE	POSITION
Victor M.G. Chaltiel	56	Chairman of the Board, Chief Executive Officer, President and Director
Leonard W. Frie	51	Executive Vice President and Chief Operating Officer
Barry C. Cosgrove	40	Vice President, General Counsel and Secretary
John E. King	37	Vice President, Finance and Chief Financial Officer

Executive officers of the Company are elected by and serve at the discretion of the Board. Set forth below is a brief description of the business experience of all executive officers other than Mr. Chaltiel, who is also a director. See "Information Concerning Members of the Board of Directors."

Leonard W. Frie has been Executive Vice President and Chief Operating Officer of the Company since August 1994. Mr. Frie was President of the Company from April 1994 through August 1994. Prior thereto, Mr. Frie served as President of Medical Ambulatory Care, Inc. and its subsidiaries since 1984.

Barry C. Cosgrove has been Vice President, General Counsel and Secretary of the Company since August 1994. Prior to joining the Company, from May 1991 to April 1994, Mr. Cosgrove served as Vice President, General Counsel and Secretary of TPC. From February 1988 to 1991, Mr. Cosgrove served as Vice President and General Counsel of McGaw Laboratories, Inc. (a subsidiary of the Kendall Company). Prior to February of 1988, Mr. Cosgrove was with the Kendall Company for seven years in numerous corporate, legal and management positions, including Assistant to the General Counsel.

John E. King has been the Vice President, Finance and Chief Financial Officer of the Company since its inception in April 1994. Prior thereto, Mr. King served in the same capacity with Medical Ambulatory Care, Inc. since May 1, 1993. From December 1990 to April 1993, he was the Chief Financial Officer for one of Tenet's general acute hospitals.

None of the executive officers has any family relationship among themselves or with any director of the Company.

#### SECTION 16(A) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) of the Exchange Act ("Section 16") requires the Company's executive officers, directors and beneficial owners of more than 10% of the Company's Common Stock (collectively, "Insiders") to file reports of ownership and changes in ownership of Common Stock of the Company with the Securities and Exchange Commission and the New York Stock Exchange, and to furnish the Company with copies of all Section 16(a) forms they file. The Company became subject to Section 16 in conjunction with the registration of its Common Stock under the Exchange Act effective October 31, 1995. Based solely on its review of the copies of such forms received by it, or written representations from certain reporting persons that no Form 5's were required for those persons, the Company believes that its Insiders complied with all applicable Section 16 filing requirements during fiscal 1997.

ITEM 11. EXECUTIVE COMPENSATION.

The following table sets forth the compensation paid or accrued by the Company to the Chief Executive Officer and to each of the executive officers for both of the fiscal years in the two-year period ended December 31, 1997, for the twelve month period ended December 31, 1995 ("Calendar 1995") and for the fiscal year ended May 31, 1995:

SUMMARY COMPENSATION TABLE

NAME AND PRINCIPAL POSITION	YEAR	ANNUAL COMPENSATION			LONG TERM COMPENSATION				ALL OTHER COMPEN- SATION (\$)
		SALARY (\$)	BONUS (\$)	OTHER ANNUAL COMPENSATION (\$)	AWARDS	SECURITIES UNDERLYING OPTIONS*	PAYOUTS	LTIP PAYOUTS (\$)	
					RESTRICTED STOCK AWARD(S) (\$)				
Victor M.G. Chaltiel	Fiscal 1997	\$288,652	\$451,776(1)	--	--	333,334	--	--	\$ 5,522(2)
Chairman of the	Fiscal 1996	285,186	438,633	--	--	166,667	--	--	5,366(3)
Board, Chief	Calendar 1995+	277,413	419,728++	--	--	--	\$3,803,800	--	9,520(4)
Executive Officer	Fiscal 1995	217,708(5)	412,500	--	--	1,477,778	--	--	207,645(6)
President and Director									
Leonard W. Frie	Fiscal 1997	182,245	143,754	--	--	111,916	--	--	14,153(7)
Executive Vice	Fiscal 1996	181,484	139,568	--	--	159,140	--	--	26,914(8)
President and	Calendar 1995+	176,535	133,551++	--	--	105,557	14,300	--	80,849(9)
Chief Operating	Fiscal 1995	165,625	131,250	--	\$99,061(10)	111,112	28,179	--	241,880(11)
Officer									
Barry C. Cosgrove	Fiscal 1997	149,817	115,004	--	--	111,916	--	--	11,582(12)
Vice President,	Fiscal 1996	145,189	111,655	--	--	116,083	--	--	10,556(13)
General Counsel	Calendar 1995+	144,480(14)	106,842++	--	--	62,500	53,625	--	8,320(15)
and Secretary	Fiscal 1995	116,777	105,000	--	--	83,333	--	--	6,695(16)
John E. King	Fiscal 1997	130,504	112,500	--	--	111,916	--	--	14,089(17)
Vice President,	Fiscal 1996	99,533	93,750	--	--	74,417	--	--	15,509(18)
Finance and Chief	Calendar 1995+	90,789	68,681++	--	--	20,833	17,875	--	42,362(19)
Financial Officer	Fiscal 1995	88,958	67,500	--	22,877(20)	27,778	2,500	--	41,487(21)

\*Includes options repriced in April 1997. See "--Report on Repricing of Options."

+ The Company changed its fiscal year from May 31 to December 31 in 1995.

++ Includes the applicable pro-rata portion of the fiscal 1995 bonus amount.

(1) Mr. Chaltiel's 1997 bonus was prepaid in December 1997.

(2) Includes (i) automobile allowance of \$5,002, and (ii) \$520 paid by the Company for an umbrella insurance policy.

(3) Includes (i) an automobile allowance of \$4,846, and (ii) \$520 paid by the Company for an umbrella insurance policy.

(4) Includes (i) an automobile allowance of \$9,000, and (ii) \$520 paid by the Company for an umbrella insurance policy.

(5) Mr. Chaltiel joined the Company as of August 11, 1994. This figure represents the amount actually earned by Mr. Chaltiel from August 11, 1994 through May 31, 1995.

(6) Includes (i) an automobile allowance of \$7,125, (ii) \$520 paid by the Company for an umbrella insurance policy, and (iii) a fee of \$200,000 received by Mr. Chaltiel from the Company prior to his employment.

(7) Includes (i) an automobile allowance of \$8,500, (ii) \$520 paid by the Company for an umbrella insurance policy, and (iii) \$5,133 in deferred compensation.

(8) Includes (i) an automobile allowance of \$8,500, (ii) \$520 paid by the Company for an umbrella insurance policy, (iii) \$4,894 in deferred compensation, and (iv) \$13,000 in payment of cash value of accrued Paid Time Off.

(9) Includes (i) an automobile allowance of \$8,500, (ii) \$520 paid by the Company for an umbrella insurance policy, (iii) a relocation fee of \$67,435, (iv) \$4,371 in deferred compensation, and (v) \$23 reimbursed by Tenet with respect to an insurance policy.

- (10) Granted by Tenet based on Mr. Frie's unvested stock options in Tenet as of August 22, 1994 and the trading value of Tenet shares on that date.
- (11) Includes (i) an automobile allowance of \$8,500, (ii) \$520 paid by the Company for an umbrella insurance policy, (iii) a relocation fee of \$88,598, (iv) \$10,524 in deferred compensation, (v) \$338 reimbursed by Tenet with respect to an insurance policy, (vi) \$900 paid by Tenet with respect to life and disability insurance under Tenet's Supplemental Executive Retirement Plan, (vii) a bonus of \$32,500 from Tenet, and (viii) a fee of \$100,000 received from Tenet.
- (12) Includes (i) an automobile allowance of \$7,800, (ii) \$520 paid by the company for an umbrella insurance policy, and (iii) \$3,262 in deferred interest income.
- (13) Includes (i) an automobile allowance of \$7,800, (ii) \$520 paid by the Company for an umbrella insurance policy, and (iii) \$2,236 in deferred interest income.
- (14) Mr. Cosgrove joined the Company as of August 8, 1994. This figure represents the amount actually earned by Mr. Cosgrove from August 8, 1994 through May 31, 1995.
- (15) Includes (i) an automobile allowance of \$7,800, and (ii) \$520 paid by the Company for an umbrella insurance policy.
- (16) Includes (i) an automobile allowance of \$6,175, and (ii) \$520 paid by the Company for an umbrella insurance policy.
- (17) Includes (i) an automobile allowance of \$7,800, (ii) \$520 paid by the Company for an umbrella insurance policy, and (iii) \$5,769 in payment of cash value of accrued Paid Time Off.
- (18) Includes (i) an automobile allowance of \$7,800, (ii) \$520 paid by the Company for an umbrella insurance policy, (iii) housing reimbursement of \$3,624, and (iv) \$3,565 in payment of cash value of accrued Paid Time Off.
- (19) Includes (i) an automobile allowance of \$7,800, (ii) \$19,025 paid by the Company for relocation expenses, (iii) housing reimbursement of \$14,990, (iv) \$520 paid by the Company for an umbrella insurance policy, and (v) \$27 reimbursed by Tenet with respect to an insurance policy.
- (20) Granted by Tenet based on Mr. King's unvested stock options in Tenet as of August 22, 1994 and the trading value of Tenet shares on that day.
- (21) Includes (i) an automobile allowance of \$7,800, (ii) \$19,025 paid by the Company for relocation expenses, (iii) \$520 paid by the Company for an umbrella insurance policy, (iv) housing reimbursement of \$13,707, and (iv) \$435 reimbursed by Tenet with respect to an insurance policy.



The following table sets forth information concerning options granted to each of the named executive officers during fiscal 1997:

OPTION/SAR GRANTS IN LAST FISCAL YEAR

NAME	NUMBER OF SECURITIES UNDERLYING OPTIONS/SARS GRANTED(1)	% OF TOTAL OPTIONS/SARS GRANTED TO EMPLOYEES IN FISCAL YEAR	EXERCISE OR BASE PRICE (\$/SH)	EXPIRATION DATE	POTENTIAL REALIZABLE VALUE AT ASSUMED ANNUAL RATES OF STOCK PRICE APPRECIATION FOR OPTION TERM	
					5% (\$)(2)	10% (\$)(2)
Victor M.G. Chaltiel....	333,334	7.4%	\$18.75	4/24/07	\$3,930,599	\$9,960,910
Leonard W. Frie.....	111,916	2.6	18.75	4/24/07	1,319,688	3,344,349
Barry C. Cosgrove.....	111,916	2.6	18.75	4/24/07	1,319,688	3,344,349
John E. King.....	111,916	2.6	18.75	4/24/07	1,319,688	3,344,349

(1) All options are nonqualified stock options and were granted under the Company's 1995 Equity Compensation Plan. Such options vest over four year periods at an annual rate of 25% beginning on the first anniversary of the date of grant.

(2) The potential realizable dollar value of a grant is the product of: (a) the difference between: (i) the product of the per-share market price at the time of the grant and the sum of one (1) plus the adjusted stock price appreciation rate (the assumed rate of appreciation compounded annually over the term of the option or SAR); and (ii) the per-share exercise price of the option or SAR; and (b) the number of securities underlying the grant at fiscal year-end. Actual gains, if any, on stock option exercises and Common Stock holdings are dependent on the future performance of the Common Stock and overall stock market conditions. There can be no assurance that the amounts reflected in this table will be achieved.

The following table sets forth information concerning the aggregate number of options exercised by each of the named executive officers during fiscal 1997:

AGGREGATED OPTION EXERCISES IN LAST FISCAL YEAR AND  
FISCAL YEAR-END OPTION VALUES

NAME	SHARES ACQUIRED ON EXERCISE(1)	VALUE REALIZED(\$)	NUMBER OF UNEXERCISED OPTIONS AT FY-END	VALUE OF UNEXERCISED IN-THE-MONEY OPTIONS AT FY-END
			EXERCISABLE/ UNEXERCISABLE(1)	EXERCISABLE/ UNEXERCISABLE(\$)(1)
Victor M.G. Chaltiel....	--	--	-- /333,334	\$ -- /\$2,916,664
Leonard W. Frie.....	--	--	105,555/111,916	2,807,763/ 979,265
Barry C. Cosgrove.....	--	--	62,500/111,916	1,662,500/ 979,265
John E. King.....	--	--	20,833/111,916	554,158/ 979,265

(1) Value is determined by subtracting the exercise price from the fair market value of \$27.50 per share (the closing price for the Company's Common Stock as reported by the New York Stock Exchange as of December 31, 1997) and multiplying the remainder by the number of underlying shares of Common Stock.

## EMPLOYMENT AGREEMENTS

Mr. Chaltiel entered into an employment agreement with the Company on August 11, 1994, pursuant to which he is employed by the Company for an initial term of three years, with one year automatic extensions at the end of each year. Such agreement is terminable by the Company at any time, subject, among other things, to severance payments as provided in the employment agreement. His base salary paid during fiscal 1997 was \$288,652 and is subject to annual review by the Board for possible increases, with a minimum increase tied to the California consumer price index. Until May 31, 1999, Mr. Chaltiel will be entitled to a yearly bonus of up to 150% of his base salary based upon the Company achieving certain EBITDA performance targets. He also may be awarded an additional bonus at the discretion of the Board if Company EBITDA targets are exceeded by more than 15%. After May 31, 1999, Mr. Chaltiel will be awarded bonuses in a manner as determined in the sole discretion of the Board, on a basis reasonably consistent with past bonuses for similar performance. Although not yet formally effected, the Company anticipates that Mr. Chaltiel's employment agreement will be amended to reflect the Company's new fiscal year end of December 31.

Mr. Chaltiel was also granted options pursuant to the Company's 1994 Equity Compensation Plan representing a total of approximately 1,477,778 shares of Common Stock. The options had an exercise price of \$0.90. By their terms, half of the options were to vest over a four-year period and the other half were to vest on the ninth anniversary of the date of grant, subject to accelerated vesting in the event that the Company satisfied certain EBITDA performance targets. On September 18, 1995, the Board and the stockholders of the Company approved an agreement dated as of the same date by and between the Company and Mr. Chaltiel pursuant to which the vesting schedule for these options was accelerated such that all of Mr. Chaltiel's outstanding options became vested and exercisable immediately. In connection with this agreement, Mr. Chaltiel agreed to exercise all of his options at that time to purchase 1,477,778 shares of Common Stock at an exercise price of \$0.90 per share. Mr. Chaltiel paid the exercise price pursuant to a \$1,330,000 four-year promissory note bearing interest at the lesser of the prime rate or 8%. This note is subject to repayment, in part or in full, to the extent of the receipt of any proceeds received by Mr. Chaltiel upon disposition of such shares of Common Stock, and Mr. Chaltiel pledged these shares as collateral for repayment of this note. Also, in accordance with the agreement, the Company agreed to advance Mr. Chaltiel funds of up to \$1,521,520 principal amount in the aggregate relating to Mr. Chaltiel's tax liability in connection with additional taxes associated with the exercise of such options. Such loans are evidenced by two additional promissory notes executed by Mr. Chaltiel. The first note for \$1,348,447 was executed concurrently with Mr. Chaltiel's exercise of his options. The second note for \$173,073 was executed as of April 15, 1996. Simultaneously with the execution of the agreement, Mr. Chaltiel and the Company entered into a Release and Pledge Agreement whereby the Company released 1,855,555 shares of Common Stock owned by Mr. Chaltiel from a previous pledge agreement and substituted the newly acquired 1,477,778 shares of Common Stock therefor.

Mr. Frie entered into an employment agreement with the Company on August 11, 1994 and Messrs. Cosgrove and King entered into employment agreements with the Company dated September 1, 1994. Pursuant to said employment agreements, Messrs. Frie, Cosgrove and King are employed by the Company for an initial term of three years, two years and one year, respectively, with one-year automatic extensions at the end of each initial term. Each such agreement is terminable by the Company at any time subject, among other things, to severance payments as set forth therein. Base salary under the employment agreements is subject to annual review by the Board for possible increases, with a minimum increase tied to the California consumer price index. These employment agreements also provide for annual bonuses, through May 31, 1999, of up to 75% of base salary, one half of which will be based on the achievement of certain EBITDA performance targets and the other half of which will be awarded at the discretion of the Board. After May 31, 1999, bonuses will be awarded in the sole discretion of the Board. Although not formally effected, the Company anticipates that the employment agreements of the above named officers will be amended to reflect the Company's new fiscal year end of December 31. Each of Messrs. Frie, Cosgrove and King have also been granted options pursuant to the Company's equity compensation plans. The Options will vest on the ninth anniversary of the date of grant, subject to accelerated vesting in the event that the Company satisfies certain EBITDA performance targets. If yearly performance targets are satisfied, the options will vest at a rate of 25% at the end of each year on the

anniversary of the date of grant. The exercise price of the options ranges from \$.90 per share to \$18.75 per share. Upon voluntary termination of employment, the Company may have the right to acquire all shares in the Company held by the terminated employee at Fair Market Value Per Share (as defined therein). Upon involuntary termination of employment, the Company may have the right to acquire all shares in the Company held by the terminated employee at 80% of Fair Market Value Per Share (as defined therein).

On December 14, 1995, the Board amended the employment contract agreement and stock option agreement of each executive officer (other than Mr. Chaltiel) to provide for the immediate vesting of all of such officers' stock options at any time following the sale of fifty percent or more of the stock or assets of the Company, or upon a merger, consolidation or reorganization in which the Company does not survive, if any of such officers' employment is terminated for any reason.

#### REPORT ON REPRICING OF OPTIONS

In April 1997, the Company's Compensation Committee determined that the purposes of the Company's equity compensation plans were not being adequately achieved with respect to those employees holding options that were above current market value and that it was essential to the best interests of the Company and the Company's stockholders that the Company retain and motivate such employees. The Compensation Committee further determined that, because the exercise prices of certain options were substantially above then-current trading prices, it would be in the best interests of the Company and the Company's stockholders to provide such optionees the opportunity to exchange their above market value options for options exercisable at the current market value. As of April 24, 1997, upon approval by the Board, the Company offered such optionees the opportunity to exchange such options for new options at an exercise price of \$18.75 per share. The last sales price of a share of Common Stock listed on the New York Stock Exchange for that day was \$18.75. Any holder accepting this offer was required to give up existing options. The repriced options vest over a three year period at an annual rate of 33 1/3% beginning April 24, 1998.

The following table sets forth information concerning the repricing of certain options held by each of the named executive officers during fiscal 1997:

#### TEN-YEAR OPTION/SAR REPRICINGS

NAME	DATE	NUMBER OF SECURITIES UNDERLYING OPTIONS/SARS	MARKET PRICE OF STOCK AT TIME OF REPRICING OR AMENDMENT (\$)	EXERCISE PRICE AT TIME OF REPRICING OR AMENDMENT (\$)	NEW EXERCISE PRICE (\$)(1)	LENGTH OF ORIGINAL OPTION TERM REMAINING AT DATE OF REPRICING OR AMENDMENT
		REPRICED OR AMENDED (#)(1)				
Victor M.G. Chaltiel....	4/24/97	100,000	31.25	39.375	31.25	9 years
Leonard W. Frie.....	4/24/97	32,150	31.25	39.375	31.25	9 years
Barry C. Cosgrove.....	4/24/97	32,150	31.25	39.375	31.25	9 years
John E. King.....	4/24/97	32,150	31.25	39.375	31.25	9 years

(1) The number of securities underlying options and exercise prices shown were subsequently adjusted to reflect the Company's five-for-three stock split on October 20, 1997 and are currently 53,583 (166,667 with regard to Mr. Chaltiel) and \$18.75, respectively.

#### COMPENSATION COMMITTEE

Peter T. Grauer, Chair  
Maris Andersons  
Regina E. Herzlinger

REPORT OF THE COMPENSATION COMMITTEE  
REGARDING COMPENSATION

The Compensation Committee (the "Committee") oversees the general compensation policies of the Company, the Company's compensation and stock incentive plans, establishes the compensation of Mr. Chaltiel, the Company's Chairman of the Board, Chief Executive Officer and President, and reviews Mr. Chaltiel's recommendations as to the compensation levels for the other executive officers.

COMPENSATION POLICY

The goal of the Company's executive compensation program is to provide a strong and direct link among stockholder values, Company performance and executive compensation through the design and implementation of a sound compensation program that will attract and retain highly qualified personnel. Compensation programs are intended to complement the Company's short- and long-term business objectives and to focus executive efforts on the fulfillment of these objectives. The Committee believes that cash compensation in the form of salary and performance-based bonuses provides Company executives with short-term rewards for success in operations, and that long-term compensation through the award of restricted stock and stock options encourages growth in management stock ownership which leads to expansion of management's stake in the long-term performance and success of the Company.

**Base Salary.** In establishing 1997 base salary levels for executive officer positions, the Committee considered the terms of the relevant employment agreements. For fiscal 1997, the Company's executive officers (other than Mr. Chaltiel) generally received raises in their annual base salary of approximately 3%. Mr. King received a raise in base salary of 20% in fiscal 1997 to adjust his base salary to approximate the levels of the Company's other executive officers. As the Committee's philosophy is to reward executive officers through bonuses, stock and stock options, increases in base salary for fiscal 1997 are minimal compared to the improved corporate performance as well as increased job responsibilities as a result of the increased size of the Company.

**Bonus.** Annual bonuses for executive officers are intended to reflect the Committee's belief that management's contribution to stockholder returns comes from maximizing earnings and the quality of those earnings. Bonus awards are based largely on the Company's attainment of EBITDA performance targets established in each executive officer's employment agreement and each executive officer's target bonus is fixed as a percentage of his base salary. For fiscal 1997, bonuses paid to the Company's executive officers (other than Mr. Chaltiel) ranged from \$112,500 to \$143,754 (or 75% of such executive officers' base salaries).

**Restricted Stock and Stock Options.** On August 5, 1994, the Company adopted the 1994 Equity Compensation Plan (the "1994 Plan"). The purpose of the 1994 Plan is to provide incentives and reward the contributions of key employees and officers for the achievement of long-term Company performance goals, as measured by earnings per share and the market value of the Common Stock. The Board set guidelines for the number and terms of stock option or restricted stock awards based on factors similar to those considered with respect to the other components of the Company's compensation program. The awards under the 1994 Plan are designed to align the interests of executives with those of the stockholders. Generally, stock options become exercisable at the end of nine years, but they may vest over a period of four years based on Company performance. The individual forfeits any installment which has not vested during the period of his or her employment. No awards were made to the executive officers under the 1994 Plan in fiscal 1997.

On October 24, 1995, the Company established the 1995 Equity Compensation Plan (the "1995 Plan"). The purpose of the 1995 Plan is to offer stock compensation to employees, directors, and other persons providing services to the Company and, accordingly, to strengthen the mutuality of interests between those persons and the Company's stockholders by providing those persons with a proprietary interest in the Company's long-term growth and financial success. Under the 1995 Plan, the Board awarded stock options in fiscal 1997 to all executive officers.

On May 15, 1997, the Company established the 1997 Equity Compensation Plan (the "1997 Plan"). The purpose of the 1997 Plan is to promote the interests of the Company and its stockholders by enabling the Company to offer employees, directors, and other persons providing services to the Company an opportunity to acquire an equity interest in the Company so as to better attract, retain and reward such persons, and accordingly, to strengthen the mutuality of interests between such persons and the Company's stockholders by providing such persons with a proprietary interest in pursuing the Company's long-term growth and financial success. No awards were made to the executive officers under the 1997 Plan in fiscal 1997.

#### COMPENSATION OF CHAIRMAN OF THE BOARD, CHIEF EXECUTIVE OFFICER AND PRESIDENT

The Committee believes that Victor M.G. Chaltiel, the Company's Chairman of the Board, Chief Executive Officer and President, provides valuable services to the Company and that his compensation should therefore be competitive with that paid to executives at comparable companies. In addition, the Committee believes that an important portion of his compensation should be based on Company performance. Mr. Chaltiel's base salary is determined pursuant to his employment agreement. Mr. Chaltiel received an increase in his base salary effective as of October 1, 1997 of \$8,762 (or 3% of base salary). The increase was based only upon a general cost of living increase as the Committee's philosophy is to reward executive officers through bonuses, stock and stock options. Mr. Chaltiel is entitled under his employment agreement to a yearly bonus of up to 150% of his base salary based upon the Company achieving certain EBITDA performance targets. He also may be awarded an additional bonus at the discretion of the Committee if Company EBITDA targets are exceeded by more than 15%. Mr. Chaltiel's bonus for fiscal 1997 was \$438,633 (or 150% of his base salary). On December 31, 1997, Mr. Chaltiel received the value of his 1998 bonus, or an additional \$451,776, to assist in paying Federal and state tax obligations.

#### COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

No executive officer or director of the Company serves as a member of the board of directors or compensation committee of any other entity which has one or more executive officers serving as a member of the Company's Board. During fiscal 1997, Messrs. Chaltiel and Andersons and Dr. Massry were officers, employees or consultants of the Company. No one other than Messrs. Andersons and Grauer served as a member of the Compensation Committee during fiscal 1997.

#### INTERNAL REVENUE CODE SECTION 162(M)

Under Section 162 of the Internal Revenue Code of 1986, as amended, the amount of compensation paid to certain executives that is deductible with respect to the Company's corporate taxes is limited to \$1,000,000 annually. It is the current policy of the Board to maximize, to the extent reasonably possible, the Company's ability to obtain a corporate tax deduction for compensation paid to executive officers of the Company to the extent consistent with the best interests of the Company and its stockholders.

#### COMPENSATION COMMITTEE

Peter T. Grauer, Chair  
Maris Andersons  
Regina E. Herzlinger

## STOCK PRICE PERFORMANCE

The following graph shows a comparison of cumulative total returns for the Company, the Standard & Poor's 400 and a Company-constructed Peer Group Index (as defined below). The graph assumes that the value of an investment in Common Stock and in each such index was \$100 on October 31, 1995 (the date the Company's Common Stock was registered under Section 12 of the Securities Exchange Act of 1934), and that all dividends have been reinvested. The Company-constructed Peer Group Index consists of the following companies: Renal Care Group, Renal Treatment Centers and Vivra (adjusted to reflect the cessation of trading in Vivra's stock as of June 12, 1997). The Company believes that the companies in the Peer Group Index are the primary competitors of the Company. The Peer Group Index is weighted for the market capitalization of each company within the group.

The comparison in the graph below is based on historical data and is not intended to forecast the possible future performance of the Company's Common Stock.

### COMPARISON OF CUMULATIVE TOTAL RETURN AMONG TOTAL RENAL CARE HOLDINGS, INC., THE STANDARD & POOR'S 400, AND TOTAL RENAL CARE HOLDINGS, INC.'S SELF-CONSTRUCTED PEER GROUP

LOGO

	OCTOBER 31, 1995	DECEMBER 29, 1995	DECEMBER 31, 1996	DECEMBER 31, 1997
-----				
Total Renal Care Holdings, Inc.....	100.00	147.24	177.91	224.95
Peer Group Index.....	100.00	116.87	136.82	212.41
S & P 400.....	100.00	105.44	127.19	163.95

The information contained above under the captions "Report of the Compensation Committee Regarding Compensation" and "Stock Price Performance" shall not be deemed to be "soliciting material" or to be "filed" with the Securities and Exchange Commission, nor shall such information be incorporated by reference into any future filing under the Securities Act or the Exchange Act, except to the extent that the Company specifically incorporates it by reference into such filing.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.

The following table sets forth information regarding the ownership of the Company's Common Stock as of December 31, 1997 by (i) all those persons known by the Company to own beneficially more than 5% of the Company's Common Stock, (ii) each director and each executive officer of the Company and (iii) all directors and executive officers as a group. Except as otherwise noted under "Certain Relationships and Related Transactions," the Company knows of no agreements among its stockholders which relate to voting or investment power over its Common Stock or any arrangement the operation of which may at a subsequent date result in a change of control of the Company.

NAME OF BENEFICIAL OWNER	NUMBER OF SHARES BENEFICIALLY OWNED	PERCENTAGE OF SHARES BENEFICIALLY OWNED
NME Properties Corp. .... c/o Tenet Healthcare Corporation 30 South La Patera Lane Goleta, California 93117	5,000,000	11.2%
Putnam Investments, Inc.(1)..... One Post Office Square Boston, Massachusetts 02109	4,111,762	9.2%
Pilgrim Baxter & Associates, Ltd..... 825 Duportail Road Wayne, Pennsylvania 19087	3,263,235	7.3%
Morgan Stanley, Dean Witter, Discover & Co. .... 1585 Broadway New York, New York 10036	2,325,456	5.2%
Denver Investment Advisors LLC..... 1225 17th Street, 26th Floor Denver, Colorado 80202	2,268,971	5.1%
Victor M.G. Chaltiel.....	934,191	2.1%
Maris Andersons.....	--	*
Barry C. Cosgrove.....	96,951	*
Leonard W. Frie.....	184,623	*
Peter T. Grauer.....	11,250	*
John E. King.....	36,020	*
Regina E. Herzlinger.....	11,250	*
Shaul G. Massry.....	16,806	*
All directors and executive officers as a group (8 persons).....	1,291,091	2.9%

- - - - -  
\* Amount represents less than 1% of the Company's Common Stock.

(1) Represents 3,981,764 shares held by Putnam Investment Management, Inc. ("PIM") and 129,998 shares held by Putnam Advisory Company, Inc. ("PAC"). PIM and PAC are each registered investment advisors that are wholly-owned by Putnam Investments, Inc. The share amounts for PIM and PAC are based upon information contained in an amendment to Schedule 13G filed with the Commission on January 27, 1998. A subsequent amendment to that Schedule 13G filed on February 6, 1998 indicated that the holdings of PIM and PAC had increased to 4,914,799 and 191,601, respectively, bringing the number of shares beneficially owned by Putnam Investments, Inc. to 5,106,400, or 11% of the Company's Common Stock as of January 31, 1998.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

Victor M.G. Chaltiel is Chairman of the Board, Chief Executive Officer, President and a Director of the Company. Pursuant to Mr. Chaltiel's employment agreement and the 1994 Plan, Mr. Chaltiel purchased 1,855,557 shares of Common Stock at \$0.90 per share during the year ended May 31, 1995. Mr. Chaltiel paid \$835,000 of the purchase price in cash, with the remainder being evidenced by a four-year promissory note bearing interest at the lesser of the prime rate or 8% per annum, which note is secured by a pledge of certain shares of stock of the Company owned by Mr. Chaltiel. In July 1995, the Board approved a one-year deferral of all scheduled principal and accrued interest payments under all outstanding promissory notes from officers of the Company, including this four-year promissory note. In September 1995, the Company and Mr. Chaltiel entered into an agreement pursuant to which Mr. Chaltiel purchased 1,477,778 shares of Common Stock upon exercise of options held by him. Mr. Chaltiel paid for such shares with a four-year promissory note for \$1,330,000 bearing interest at the lesser of the prime rate or 8%. This note is subject to repayment, in part or in full, to the extent of the receipt of proceeds received by Mr. Chaltiel upon disposition of such shares of Common Stock, and Mr. Chaltiel pledged these shares as collateral for repayment of this note. The Company also agreed to advance Mr. Chaltiel funds of up to \$1,521,520 principal amount in the aggregate relating to Mr. Chaltiel's tax liability in connection with the shares. Such loans are evidenced by two additional promissory notes executed by Mr. Chaltiel. The first note for \$1,348,447 was executed concurrently with Mr. Chaltiel's exercise of his options in September 1995. The second note for \$173,073 was executed as of April 15, 1996. Simultaneously with the execution of the agreement, Mr. Chaltiel and the Company entered into a Release and Pledge Agreement whereby the Company released 1,855,557 shares of Common Stock owned by Mr. Chaltiel from a previous pledge agreement and substituted the newly acquired 1,477,778 shares of Common Stock therefor.

Certain of the Company's officers and employees have received loans from the Company in connection with the purchase of shares of Common Stock. All of the loans have similar terms. The loans bear interest at the lower of 8% or the prime rate, and are secured by all of the borrower's interests in Common Stock of the Company, including all vested stock options. When made, the loans had a four-year term and one quarter of the original principal amount thereof plus all accrued interest thereon had to be paid annually, subject to the limitation that the borrower was not required to make any payment that exceeded 50% of the after-tax proceeds of such borrower's bonus from the Company (based on maximum tax rates then in effect). To date, the Board has approved deferrals of all scheduled principal and accrued interest payments under all such loans. No other terms of the loans have been changed.

As of December 31, 1997, Leonard W. Frie, Barry C. Cosgrove and John E. King had loans outstanding from the Company with principal amounts of \$100,000, \$70,000 and \$25,000, respectively (with respect to Mr. Cosgrove, \$50,000 was borrowed to purchase shares of Common Stock and \$20,000 was borrowed for relocation costs). Victor M.G. Chaltiel had an outstanding loan of \$835,000 prior to the addition in September 1995 of \$2,678,447 pursuant to similar loans in connection with Mr. Chaltiel's exercise of options for 1,477,778 shares of Common Stock and related personal income tax obligations, as described above. These loans are secured by a pledge of 1,444,445 shares of Common Stock. Mr. Chaltiel received a similar loan from the Company on April 15, 1996, in the amount of \$173,073, in connection with additional taxes associated with the exercise of such options.

Maris Andersons, a Director of the Company, serves as a consultant to the Company. He has been granted options, vesting over four years, to purchase an aggregate of 101,972 shares of Common Stock in consideration for these services. As of December 31, 1997, Mr. Andersons has exercised 27,778 of said options leaving a balance of 74,194 options to purchase shares of Common Stock.

Shaul G. Massry, a Director of the Company, serves as a consultant to the Company. In addition to certain compensation as a member of the Board, Dr. Massry receives \$50,000 per year and has been granted options, vesting over four years, to purchase an aggregate of 44,722 shares of Common Stock in consideration for these services. As of December 31, 1997, Dr. Massry has exercised 11,110 of such options leaving a balance of 33,612 options to purchase shares of Common Stock.



The Company, DLJ Merchant Banking Partners, L.P. ("DLJMBP"), certain members of management and NME Properties Corp. ("NME"), a wholly-owned subsidiary of Tenet, entered into a shareholders' agreement (as amended, the "Shareholders' Agreement") in August 1994 pursuant to which, among other provisions, DLJMBP had the right to nominate four of the five members of the Company's Board. Although this right has terminated, an affiliate of DLJMBP, Peter T. Grauer, continues to serve on the Company's Board. The Shareholders' Agreement further provides for certain registration rights and for restrictions on transfers of Common Stock, certain rights of first refusal in favor of DLJMBP in the event NME proposes to transfer shares of Common Stock and certain rights and obligations of NME to participate in transfers of shares by DLJMBP. DLJ and certain of its affiliates from time to time perform various investment banking and other services for the Company, for which the Company pays customary consideration.

The Company has entered into indemnity agreements with each of its directors and all of its officers, which agreements require the Company, among other things, to indemnify them against certain liabilities that may arise by reason of their status or service as directors, officers, employees or agents of the Company (other than liabilities arising from conduct in bad faith or which is knowingly fraudulent or deliberately dishonest), and, under certain circumstances, to advance their expenses incurred as a result of proceedings brought against them.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K.

(a) Documents filed as part of this Report:

(1) Index to Financial Statements:

	PAGE
Report of Independent Accountants of Price Waterhouse LLP	F-1
Consolidated Balance Sheets as of December 31, 1996 and December 31, 1997	F-2
Consolidated Statements of Income for year ended May 31, 1995, the seven months ended December 31, 1994 (unaudited) and December 31, 1995 and the years ended December 31, 1995 (unaudited), December 31, 1996 and December 31, 1997	F-3
Consolidated Statements of Stockholders' Equity for the year ended May 31, 1995, the seven months ended December 31, 1995 and the years ended December 31, 1996 and December 31, 1997	F-4
Consolidated Statements of Cash Flows for year ended May 31, 1995, the seven months ended December 31, 1994 (unaudited) and December 31, 1995 and the years ended December 31, 1995 (unaudited), December 31, 1996 and December 31, 1997	F-5
Notes to Consolidated Financial Statements	F-6

(2) Index to Financial Statement Schedules:

Report of Independent Accountants on Financial Statement	S-1
Schedule of Price Waterhouse LLP	S-2
Schedule II--Valuation and Qualifying Accounts	

(3)(a) Exhibits:

- 3.1 Amended and Restated Certificate of Incorporation of the Company, dated December 4, 1995.@@
- 3.2 Certificate of Amendment of Certificate of Incorporation of the Company, dated February 26, 1998.X
- 3.3 Bylaws of the Company, dated October 6, 1995.+
- 4.1 Shareholders Agreement, dated August 11, 1994 between DLJMB, DLJIP, DLJOP, DLJMBF, NME Properties, Continental Bank, as voting trustee, and the Company.##
- 4.2 Agreement and Amendment, dated as of June 30, 1995, between DLJMBP, DLJIP, DLJOP, DLJMBF, DLJESC, Tenet, the Company, Victor M.G. Chaltiel, the Putnam Purchasers, the Crescent Purchasers and the Harvard Purchasers, relating to the Shareholders Agreement dated as of August 11, 1994 between DLJMB, DLJIP, DLJOP, DLJMBF, NME Properties, Continental Bank, as voting trustee, and the Company.##
- 10.1 Credit Agreement by and among the Company, the Lenders party thereto, BNY Capital Markets, Inc. and Donaldson Lufkin & Jenrette Securities Corporation as Arrangers, DLJ Capital Funding, Inc. as Documentation Agent and The Bank of New York as Administrative Agent, dated as of October 11, 1996 (the "TRCH Credit Facility").@
- 10.2 Guaranty by Total Renal Care, Inc. to The Bank of New York, as Administrative Agent, pursuant to the TRCH Credit Facility.@
- 10.3 Subscription Agreement dated May 26, 1994 between DLJMB, DLJIP, DLJOP, DLJMBF, NME Properties, Tenet and the Company.#
- 10.4 Services Agreement dated August 11, 1994 between the Company and Tenet.##

- 10.5 Noncompetition Agreement dated August 11, 1994 between the Company and Tenet.##
- 10.6 Employment Agreement dated as of August 11, 1994 by and between the Company and Victor M.G. Chaltiel (with forms of Promissory Note and Pledge and Stock Subscription Agreement attached as exhibits thereto) (the "Chaltiel Employment Agreement").##\*
- 10.7 Amendment to Chaltiel Employment Agreement, dated as of August 11, 1994.##\*
- 10.8 Employment Agreement dated as of September 1, 1994 by and between the Company and Barry C. Cosgrove.##\*
- 10.9 Employment Agreement dated as of August 11, 1994 by and between the Company and Leonard W. Frie (the "Frie Employment Agreement").##\*
- 10.10 Amendment to Frie Employment Agreement, dated as of October 11, 1994.##\*
- 10.11 Employment Agreement dated as of September 1, 1994 by and between the Company and John E. King.##\*
- 10.12 First Amended and Restated 1994 Equity Compensation Plan (the "1994 Plan") of the Company (with form of Promissory Note and Pledge attached as an exhibit thereto), dated August 5, 1994.##\*
- 10.13 Form of Stock Subscription Agreement relating to the 1994 Plan.##\*
- 10.14 Form of Purchased Shares Award Agreement relating to the 1994 Plan.##\*
- 10.15 Form of Nonqualified Stock Option relating to the 1994 Plan.##\*
- 10.16 1995 Equity Compensation Plan.+\*
- 10.17 Employee Stock Purchase Plan.+\*
- 10.18 Option Exercise and Bonus Agreement dated as of September 18, 1995 between the Company and Victor M.G. Chaltiel.+\*
- 10.19 1997 Equity Compensation Plan.\*\*
- 10.20 Revolving Credit Agreement, dated as of October 24, 1997, by and among the Company, the lenders party thereto, DLJ Capital Funding, Inc., as Syndication Agent, First Union National Bank, as Documentation Agent, and The Bank of New York, as Administrative Agent (the "Revolving Credit Agreement").@@@
- 10.21 Amendment No. 1 and Consent No. 1, dated as of December 1, 1997, to the Revolving Credit Agreement.@@@
- 10.22 Term Loan Agreement, dated as of October 24, 1997, by and among the Company, the lenders party thereto, DLJ Capital Funding, Inc., as Syndication Agent, First Union National Bank, as Documentation Agent, and The Bank of New York, as Administrative Agent (the "Term Loan Agreement").@@@
- 10.23 First Amendment, dated December 1, 1997, to the Term Loan Agreement.@@@
- 10.24 Subsidiary Guaranty (the "Subsidiary Guaranty") dated as of October 24, 1997 by Total Renal Care, Inc., TRC West, Inc. and Total Renal Care Acquisition Corp. in favor of and for the benefit of The Bank of New York, as Collateral Agent, the lenders to the Revolving Credit Agreement, the lenders to the Term Loan Agreement, the Term Agent (as defined therein), the Acknowledging Interest Rate Exchangers (as defined therein) and the Acknowledging Currency Exchangers (as defined therein).@@@
- 10.25 Borrower Pledge Agreement dated as of October 24, 1997 and entered into by and between the Company, and The Bank of New York, as Collateral Agent, the lenders to the Revolving Credit Agreement, the lenders to the Term Loan Agreement, the Term Agent (as defined therein), the Acknowledging Interest Rate Exchangers (as defined therein) and the Acknowledging Currency Exchangers (as defined therein).@@@

- 10.26 Form of Subsidiary Pledge Agreement dated as of October 24, 1997 by Total Renal Care, Inc., TRC West, Inc. and Total Renal Care Acquisition Corp., and The Bank of New York, as Collateral Agent, the lenders to the Revolving Credit Agreement, the lenders to the Term Loan Agreement, the Term Agent (as defined therein), the Acknowledging Interest Rate Exchangers (as defined therein) and the Acknowledging Currency Exchangers (as defined therein).@@@
- 10.27 Agreement and Plan of Merger dated as of November 18, 1997 by and among TRCH, Nevada Acquisition Corp., a Delaware corporation and wholly-owned subsidiary of TRCH, and RTC.###
- 10.28 Second Amendment, dated January 13, 1998, to the Term Loan Agreement.X
- 10.29 Amendment No. 2 and Consent No. 2 to the Revolving Credit Agreement and First Amendment to the Subsidiary Guaranty dated February 17, 1998.X
- 10.30 Third Amendment to the Term Loan Agreement and First Amendment to the Subsidiary Guaranty dated February 17, 1998.X
- 10.31 Special Purpose Option Plan++
- 10.32 Indenture, dated June 12, 1996 by RTC to PNC Bank including form of RTC Note (the "Indenture").\*\*\*
- 10.33 First Supplemental Indenture, dated as of February 27, 1998, among RTC, TRCH and PNC Bank under the Indenture.X
- 10.34 Second Supplemental Indenture, dated as of March 31, 1998, among RTC, TRCH and PNC Bank under the Indenture.X
- 10.35 Guaranty, entered into as of March 31, 1998, by TRCH in favor of and for the benefit of PNC Bank.X
- 21 List of Subsidiaries of the Company.X
- 23.1 Consent of Price Waterhouse LLP.X
- 24 Powers of Attorney with respect to the Company (included on page II-1 hereof). X
- 27 Financial Data Schedule.X

- -----

X Included in this filing.

@ Filed on October 18, 1996 as an exhibit to the Company's Current Report on Form 8-K.

@@ Filed on March 18, 1996 as an exhibit to the Company's Transitional Report on Form 10-K for the transition period from June 1, 1995 to December 31, 1995.

@@@ Filed on December 19, 1997 as an exhibit to the Company's Current Report on Form 8-K.

+ Filed on October 24, 1995 as an exhibit to Amendment No. 2 to the Company's Registration Statement on Form S-1 (Registration Statement No. 33-97618).

++ Filed on February 25, 1998 as an exhibit to the Company's Registration Statement on Form S-8 (Registration Statement No. 333-46887).

# Filed on June 6, 1994 as an exhibit to the Company's Registration Statement on Form S-1 (Registration Statement No. 33-79770).

## Filed on August 29, 1995 as an exhibit to the Company's Form 10-K for the year ended May 31, 1995.

### Filed on December 19, 1997 as Annex A to the Company's Registration Statement on Form S-4 (Registration Statement No. 333-42653).

\* Management contract or executive compensation plan or arrangement.

\*\* Filed on August 29, 1997 as an exhibit to the Company's Registration Statement on Form S-8 (Registration Statement No. 333-34695).

\*\*\* Filed as an exhibit to RTC's Form 10-Q for the quarter ended June 30, 1996.

(b) Reports on Form 8-K:

Current Report on Form 8-K, dated November 21, 1997, reporting under Item 5 the issuance by TRCH of a press release in connection with the Merger.

Current Report on Form 8-K, dated December 19, 1997, reporting under Item 7: (i) the Audited Financial Statements of the Nephrology Services Business of Caremark International, Inc., (ii) the Audited Financial Statements of New West Dialysis, Inc., (iii) the Audited Combined Financial Statements of Southfield Dialysis Facility, P.C., North Oakland Dialysis Facility, P.C., Macomb Kidney Center, P.C., and Novi Kidney Center, P.C., (iv) Audited Financial Statements of Dialysis Care of North Carolina, (v) Audited Financial Statements of the Renal Dialysis Business of the Rogosin Institute, Inc. and (vi) certain Unaudited Pro Forma Financial Statements.

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and Stockholders of  
Total Renal Care Holdings, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, of stockholders' equity, and of cash flows present fairly, in all material respects, the financial position of Total Renal Care Holdings, Inc. and its subsidiaries at December 31, 1996 and 1997, and the results of their operations and their cash flows for the year ended May 31, 1995, the seven months ended December 31, 1995 and the years ended December 31, 1996 and 1997 in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

PRICE WATERHOUSE LLP  
Seattle, Washington  
February 16, 1998, except as to Note 17  
which is as of March 30, 1998

## TOTAL RENAL CARE HOLDINGS, INC.

## CONSOLIDATED BALANCE SHEETS

	DECEMBER 31, 1996	DECEMBER 31, 1997
ASSETS		
Cash and cash equivalents.....	\$ 19,881,000	\$ 5,400,000
Patient accounts receivable, less allowance for doubtful accounts of \$7,911,000 and \$11,892,000, respectively.....	91,009,000	152,481,000
Receivable from Tenet.....	347,000	534,000
Inventories.....	6,045,000	8,743,000
Deferred income taxes.....	3,233,000	6,146,000
Prepaid expenses and other current assets.....	10,771,000	12,746,000
	-----	-----
Total current assets.....	131,286,000	186,050,000
Property and equipment, net.....	58,266,000	100,061,000
Notes receivable from related parties.....	1,919,000	11,344,000
Other long-term assets.....	1,992,000	8,148,000
Intangible assets, net.....	180,617,000	389,737,000
	-----	-----
	\$374,080,000	\$695,340,000
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Accounts payable.....	\$ 9,818,000	\$ 14,547,000
Employee compensation and benefits.....	12,360,000	15,987,000
Other accrued liabilities.....	7,745,000	7,221,000
Current portion of long-term obligations.....	2,064,000	2,021,000
	-----	-----
Total current liabilities.....	31,987,000	39,776,000
	-----	-----
Long-term debt.....	102,552,000	356,563,000
	-----	-----
Deferred income taxes.....	2,868,000	5,100,000
	-----	-----
Other long-term liabilities.....	993,000	1,150,000
	-----	-----
Minority interests.....	4,714,000	19,079,000
	-----	-----
Commitments and contingencies (Notes 8, 9 and 13)		
Stockholders' equity		
Preferred stock, (\$.001 par value; 5,000,000 shares authorized; none issued or outstanding)..	--	--
Common stock (\$.001 par value; 195,000,000 shares authorized; 44,121,637 and 44,589,645 shares issued and outstanding).....	44,000	45,000
Additional paid-in capital.....	255,879,000	261,810,000
Notes receivable from stockholders.....	(2,827,000)	(3,030,000)
Retained (deficit) earnings.....	(22,130,000)	14,847,000
	-----	-----
Total stockholders' equity.....	230,966,000	273,672,000
	-----	-----
	\$374,080,000	\$695,340,000
	=====	=====

See accompanying notes to consolidated financial statements.

TOTAL RENAL CARE HOLDINGS, INC.  
CONSOLIDATED STATEMENTS OF INCOME

	YEAR ENDED MAY 31, 1995	SEVEN MONTHS ENDED DECEMBER 31, ----- 1994      1995 (UNAUDITED)		YEAR ENDED DECEMBER 31, ----- 1995      1996      1997 (UNAUDITED)		
Net operating revenues..	\$98,968,000	\$53,593,000	\$89,711,000	\$134,843,000	\$272,947,000	\$438,205,000
Operating expenses						
Facilities.....	65,583,000	36,012,000	57,406,000	86,977,000	183,987,000	292,495,000
General and administrative.....	9,115,000	4,916,000	7,645,000	11,844,000	19,267,000	29,832,000
Provision for doubtful accounts.....	2,371,000	1,363,000	1,811,000	2,819,000	5,496,000	8,896,000
Depreciation and amortization.....	4,740,000	2,586,000	4,383,000	6,537,000	15,368,000	27,124,000
Total operating expenses.....	81,809,000	44,877,000	71,245,000	108,177,000	224,118,000	358,347,000
Operating income.....	17,159,000	8,716,000	18,466,000	26,666,000	48,829,000	79,858,000
Interest expense, net of capitalized interest...	(7,447,000)	(3,378,000)	(6,291,000)	(10,117,000)	(7,052,000)	(15,678,000)
Interest income.....	244,000	78,000	707,000	873,000	1,877,000	2,440,000
Income before income taxes, minority interests and extraordinary item....	9,956,000	5,416,000	12,882,000	17,422,000	43,654,000	66,620,000
Income taxes.....	3,511,000	1,933,000	4,631,000	6,209,000	16,351,000	25,141,000
Income before minority interests and extraordinary item....	6,445,000	3,483,000	8,251,000	11,213,000	27,303,000	41,479,000
Minority interests in income of consolidated subsidiaries.....	1,593,000	833,000	1,784,000	2,544,000	3,578,000	4,502,000
Income before extraordinary item....	4,852,000	2,650,000	6,467,000	8,669,000	23,725,000	36,977,000
Extraordinary loss related to early extinguishment of debt, net of tax.....			2,555,000	2,555,000	7,700,000	
Net income.....	\$ 4,852,000	\$ 2,650,000	\$ 3,912,000	\$ 6,114,000	\$ 16,025,000	\$ 36,977,000
Earnings per common share:						
Net income before extraordinary item....	\$ 0.27	\$ 0.18	\$ 0.23	\$ 0.35	\$ 0.57	\$ 0.83
Extraordinary loss.....			(0.09)	(0.10)	(0.19)	
Net income.....	\$ 0.27	\$ 0.18	\$ 0.14	\$ 0.25	\$ 0.38	\$ 0.83
Weighted average number of common shares outstanding.....	18,050,000	14,692,000	27,600,000	24,742,000	41,695,000	44,304,000
Earnings per common share--assuming dilution:						
Net income before extraordinary item....	\$ 0.24	\$ 0.16	\$ 0.22	\$ 0.32	\$ 0.55	\$ 0.82
Extraordinary loss.....			(0.09)	(0.09)	(0.18)	
Net income.....	\$ 0.24	\$ 0.16	\$ 0.13	\$ 0.23	\$ 0.37	\$ 0.82
Weighted average number of common shares and equivalents outstanding--assuming dilution.....	19,834,000	16,456,000	29,707,000	26,912,000	42,988,000	45,302,000

See accompanying notes to consolidated financial statements.



## TOTAL RENAL CARE HOLDINGS, INC.

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	NOTES RECEIVABLE FROM STOCKHOLDERS	RETAINED EARNINGS (DEFICIT)	TOTAL
	SHARES	AMOUNT				
Balance at May 31, 1994.....	111,112				\$34,733,000	\$ 34,733,000
Shares issued to Tenet..	4,888,890	\$ 4,000				4,000
Shares issued in change of control:						
DLJMB.....	11,666,667	12,000	\$ 10,488,000			10,500,000
Employees.....	2,077,778	2,000	1,868,000	\$ (995,000)		875,000
Shares issued in offering.....	1,000,000	1,000	899,000			900,000
Stock issuance costs....			(2,172,000)			(2,172,000)
Dividend paid to Tenet:						
Cash.....					(75,500,000)	(75,500,000)
Intercompany receivable.....					(6,152,000)	(6,152,000)
Shares issued in acquisitions.....	495,773	1,000	445,000			446,000
Shares issued to employees and others...	1,275,420	1,000	1,147,000	(513,000)		635,000
Net income.....					4,852,000	4,852,000
Balance at May 31, 1995.....	21,515,640	21,000	12,675,000	(1,508,000)	(42,067,000)	(30,879,000)
Net proceeds from initial public offering.....	11,500,000	12,000	98,282,000			98,294,000
Shares and options issued in acquisitions.....	1,238,033	1,000	5,334,000			5,335,000
Shares issued to employees and others...	46,117		59,000	(13,000)		46,000
Options exercised.....	1,744,443	2,000	1,564,000	(1,330,000)		236,000
Conversion of mandatorily redeemable common stock.....	1,136,112	1,000	3,989,000			3,990,000
Payments on notes receivable, net of interest accrued.....				78,000		78,000
Income tax benefit related to stock options exercised.....			1,792,000			1,792,000
Net income.....					3,912,000	3,912,000
Balance at December 31, 1995.....	37,180,345	37,000	123,695,000	(2,773,000)	(38,155,000)	82,804,000
Net proceeds from stock offerings.....	6,666,667	7,000	128,311,000			128,318,000
Shares issued in acquisitions.....	161,095		2,810,000			2,810,000
Shares issued to employees and others...	1,883		15,000			15,000
Options exercised.....	111,647		110,000			110,000
Interest accrued on notes receivable, net of payments.....				(54,000)		(54,000)
Income tax benefit related to stock options exercised.....			938,000			938,000
Net income.....					16,025,000	16,025,000
Balance at December 31, 1996.....	44,121,637	44,000	255,879,000	(2,827,000)	(22,130,000)	230,966,000
Shares issued in acquisitions.....	17,613		273,000			273,000
Shares issued to employees and others...	174,775		1,773,000			1,773,000
Options exercised.....	275,620	1,000	711,000			712,000
Interest accrued on notes receivable, net of payments.....				(203,000)		(203,000)
Income tax benefit related to stock options exercised.....			3,174,000			3,174,000
Net income.....					36,977,000	36,977,000
Balance at December 31, 1997.....	44,589,645	\$45,000	\$261,810,000	\$(3,030,000)	\$14,847,000	\$273,672,000
	=====	=====	=====	=====	=====	=====

See accompanying notes to consolidated financial statements.

## TOTAL RENAL CARE HOLDINGS, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

	YEAR ENDED MAY 31, 1995	SEVEN MONTHS ENDED DECEMBER 31,		YEAR ENDED DECEMBER 31,		
		1994 (UNAUDITED)	1995	1995 (UNAUDITED)	1996	1997
Cash flows from operating activities						
Net income.....	\$ 4,852,000	\$ 2,650,000	\$ 3,912,000	\$ 6,114,000	\$ 16,025,000	\$ 36,977,000
Adjustments to reconcile net income to net cash provided by operating activities:						
Depreciation and amortization.....	4,740,000	2,586,000	4,383,000	6,537,000	15,368,000	27,124,000
Extraordinary loss....			4,258,000	4,258,000	12,623,000	
Non-cash interest....	6,947,000	3,274,000	5,228,000	8,901,000	4,396,000	
Deferred income taxes.....	(716,000)	16,000	(469,000)	(726,000)	667,000	(681,000)
Provision for doubtful accounts.....	2,371,000	1,363,000	1,811,000	2,819,000	5,496,000	8,896,000
(Gain) loss on disposition of property and equipment.....	(34,000)		(144,000)	(146,000)	(20,000)	10,000
Minority interests in income of consolidated subsidiaries.....	1,593,000	833,000	1,784,000	2,544,000	3,578,000	4,502,000
Changes in operating assets and liabilities, net of effect of acquisitions:						
Accounts receivable..	(9,547,000)	(4,023,000)	(15,256,000)	(20,801,000)	(32,939,000)	(74,715,000)
Inventories.....	(122,000)	(303,000)	(331,000)	(150,000)	(1,976,000)	(1,328,000)
Prepaid expenses and other current assets.....	(856,000)	(261,000)	(134,000)	(532,000)	(7,638,000)	1,408,000
Other long-term assets.....			(300,000)	(300,000)		
Accounts payable....	(536,000)	728,000	205,000	(968,000)	(2,688,000)	447,000
Employee compensation and benefits.....	1,994,000	2,000	(622,000)	1,090,000	4,995,000	3,583,000
Other accrued liabilities.....	4,383,000	544,000	461,000	4,182,000	1,096,000	(448,000)
Income taxes payable.....		465,000	277,000	(931,000)	(314,000)	
Other long-term liabilities.....		107,000	1,214,000	916,000	(222,000)	13,000
Net cash provided by operating activities.....	15,069,000	7,981,000	6,277,000	12,807,000	18,447,000	5,788,000
Cash flow from investing activities						
Purchases of property and equipment.....	(3,835,000)	(860,000)	(3,748,000)	(6,880,000)	(25,464,000)	(36,878,000)
Additions to intangible assets....	(358,000)	(159,000)	(972,000)	(1,167,000)	(7,530,000)	(23,268,000)
Cash paid for acquisitions, net of cash acquired.....	(22,476,000)	(5,722,000)	(28,303,000)	(45,056,000)	(138,202,000)	(200,624,000)
Investment in other long-term assets ....			(972,000)	(972,000)	(46,000)	(2,935,000)
Issuance of long-term notes receivable.....			(1,379,000)	(1,379,000)	(540,000)	(12,502,000)
Proceeds from disposition of property and equipment.....	62,000	28,000	244,000	273,000	236,000	10,000
Net cash used in investing activities.....	(26,607,000)	(6,713,000)	(35,130,000)	(55,181,000)	(171,546,000)	(276,197,000)
Cash flows from financing activities						
Advances from Tenet...	2,874,000	3,499,000				
Proceeds from issuance of note payable.....			258,000	258,000	107,000	553,000

Principal payments on long-term obligations.....	(367,000)	(11,000)	(880,000)	(1,238,000)	(918,000)	(15,551,000)
Cash dividends paid to Tenet.....	(75,500,000)	(75,500,000)				
Net proceeds from debt offering.....	66,841,000	66,140,000				
Cash paid to retire bonds.....			(31,912,000)	(31,912,000)	(68,499,000)	
Proceeds from bank credit facility.....	13,253,000		21,341,000	31,295,000	209,335,000	268,000,000
Payment of bank credit facility.....	(4,000,000)		(31,625,000)	(31,625,000)	(124,335,000)	
Net proceeds from issuance of common stock.....	10,742,000	10,810,000	98,941,000	98,965,000	128,443,000	2,485,000
Income tax benefit related to stock options exercised....			1,792,000	1,792,000	938,000	3,174,000
Cash received on notes receivable from stockholders.....			175,000	175,000	170,000	35,000
Distributions to minority interests...	(1,708,000)	(723,000)	(1,102,000)	(2,087,000)	(2,442,000)	(2,768,000)
	-----	-----	-----	-----	-----	-----
Net cash provided by financing activities.....	12,135,000	4,215,000	56,988,000	65,623,000	142,799,000	255,928,000
	-----	-----	-----	-----	-----	-----
Net increase (decrease) in cash.....	597,000	5,483,000	28,135,000	23,249,000	(10,300,000)	(14,481,000)
Cash and cash equivalents at beginning of period...	1,449,000	1,449,000	2,046,000	6,932,000	30,181,000	19,881,000
	-----	-----	-----	-----	-----	-----
Cash and cash equivalents at end of period.....	\$ 2,046,000	\$ 6,932,000	\$ 30,181,000	\$ 30,181,000	\$ 19,881,000	\$ 5,400,000
	=====	=====	=====	=====	=====	=====

Supplemental cash flow information (Note 15)

See accompanying notes to consolidated financial statements

TOTAL RENAL CARE HOLDINGS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Total Renal Care Holdings, Inc. (the "Company") operates kidney dialysis facilities and provides related medical services in Medicare certified dialysis facilities in various geographic sectors of the United States, Puerto Rico, Europe and Guam.

The Company was a wholly-owned subsidiary of Tenet Healthcare Corporation ("Tenet," formerly National Medical Enterprises, Inc.) until August 1994. In August 1994, the Company completed a public offering of senior subordinated notes and common stock, the proceeds of which were used to partially fund a dividend to Tenet. Immediately after payment of the dividend, Donaldson, Lufkin, Jenrette Merchant Banking Funding, Inc. and certain of its affiliates ("DLJMB") and certain members of management acquired newly issued common stock of the Company to effect a change in control of the Company. Although there was a change in control, the Company's accounts were not adjusted from their historical bases due to the significant continuing ownership interest of Tenet.

On February 27, 1998, the Company completed its merger with Renal Treatment Centers, Inc. (the "Merger"). The Merger was treated as a pooling of interests for accounting purposes (see Note 17).

Basis of presentation

The consolidated financial statements include the accounts of Total Renal Care Holdings, Inc. and its wholly-owned and majority-owned corporate subsidiaries and partnership investments. All significant intercompany transactions and balances have been eliminated in consolidation.

Net operating revenues

Revenues are recognized when services and related products are provided to patients in need of ongoing life sustaining kidney dialysis treatments. Operating revenues consist primarily of dialysis and ancillary fees from patient treatments. These amounts are reported at the amounts expected to be realized from governmental and third-party payors, patients and others for services provided. Appropriate allowances are established based upon credit risk of specific third-party payors, historical trends and other factors and are reflected in the provision for doubtful accounts as a component of operating expenses in the consolidated statements of income.

During the years ended May 31, 1995, the seven months ended December 31, 1995 and the years ended December 31, 1996 and 1997, the Company received approximately 70%, 67%, 67% and 65%, respectively, of its dialysis revenues from Medicare and Medicaid programs. Accounts receivable from Medicare and Medicaid amounted to \$40,159,000 and \$79,824,000 as of December 31, 1996, and 1997, respectively. Medicare historically pays approximately 80% of government established rates for services provided by the Company. The remaining 20% is typically paid by state Medicaid programs, private insurance companies or directly by the patients receiving the services.

Medicare and Medicaid programs funded by the U.S. government generally reimburse the Company under prospective payment systems at amounts different from the Company's established private rates. Revenues under these programs are generally recognized at prospective rates which are subject to periodic adjustment by federal and state agencies. The Company bills non-governmental third-party payors at established private rates. The Company has contracts for the provision of dialysis services to members of certain managed care organizations which generally include rate provisions at less than the established private rates.

In August 1993, the provisions of the Omnibus Budget Reconciliation Act of 1993 ("OBRA 93") became effective. The OBRA 93 provisions were originally interpreted by the Health Care Financing Administration ("HCFA") to modify the requirements that employer group health sponsored insurance plans (private payors)

TOTAL RENAL CARE HOLDINGS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

be the primary payor for end-stage renal disease ("ESRD") patients who subsequently become dually entitled to Medicare benefits because of ESRD following initial eligibility under age or disability provisions. In July 1994, HCFA instructed the Medicare fiscal intermediaries to retroactively apply the provisions of OBRA 93 to August 10, 1993. In April 1995, HCFA issued instructions of clarification to the fiscal intermediaries that it had misinterpreted the OBRA regulations and that Medicare would continue as the primary payor after dual eligibility was achieved under the ESRD provision. In January 1998, a permanent injunction was issued by a federal court preventing HCFA from retroactively applying its reinterpretation of the OBRA 93 regulations as unlawful retroactive rule-making. Accordingly, the Company has recognized as revenue payments from private payors in excess of the revenue previously recognized at lower rates which are attributable to such patients.

As a Medicare and Medicaid provider, the Company is subject to extensive regulation by both the federal government and the states in which the Company conducts its business. Due to heightened awareness of federal and state budgets, scrutiny is being placed on the health care industry, potentially subjecting the Company to regulatory investigation and changes in billing procedures.

The provisions of the Kennedy-Kassebaum legislation issued January 1, 1997 may limit the Company's ability to pay for policy premiums for patients even with proven financial hardship. However, the Company believes that the bill did not intend to limit the Company's ability to pay premiums for insurance coverage to third-party or governmental payors. In the Fall of 1997, the Office of Inspector General of the HHS issued an advisory opinion which would allow the Company to make grants to a foundation that may provide for such premium payments on behalf of ESRD patients. In addition, legislation is currently pending which would permit the Company to pay premiums for insurance coverage for patients with proven financial hardship.

Cash and cash equivalents

Cash equivalents are highly liquid investments with original maturities of three months or less.

Inventories

Inventories are stated at the lower of cost (first-in, first-out) or market and consist principally of drugs and dialysis related supplies.

Property and equipment

Property and equipment are stated at cost. Maintenance and repairs are charged to expense as incurred. Depreciation and amortization expense are computed using the straight-line method over the useful lives of the assets estimated as follows: buildings, 20 to 40 years; leaseholds and improvements, over the shorter of their estimated useful life or the lease term; and equipment, three to 15 years.

Capitalized Interest

The Company capitalizes interest associated with the costs of significant facility expansion and construction. Interest is capitalized by using an interest rate which is equal to the weighted average borrowing rate on the Company's long-term debt. Approximately \$685,000 in interest expense was capitalized for the year ended December 31, 1997.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

Intangible assets

Business acquisition costs allocated to patient lists are amortized over five to seven years using the straight-line method. Business acquisition costs allocated to covenants not to compete are amortized over the terms of the agreements, typically seven to ten years, using the straight-line method. Deferred debt issuance costs are amortized over the term of the debt using the effective interest method. Pre-opening and development costs, included in other intangible assets, are amortized over five years.

The excess of aggregate purchase price over the fair value of net assets of businesses acquired is recorded as goodwill. Goodwill is amortized over 15 to 40 years using the straight-line method.

The carrying value of intangible assets is assessed for any permanent impairment by evaluating the operating performance and future undiscounted cash flows from operations of the underlying businesses. Adjustments are made if the sum of the expected future undiscounted net cash flows is less than book value. Statement of Financial Accounting Standards No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of ("SFAS 121"), requires that long-lived assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of assets may not be recoverable.

Income taxes

The Company accounts for income taxes using an asset and liability approach, which requires recognition of deferred income taxes for all temporary differences between the tax and financial reporting bases of the Company's assets and liabilities based on enacted tax rates applicable to the periods in which the differences are expected to be recovered or settled.

Following the change in control described above, the Company's results of operations were no longer included in Tenet's consolidated federal and applicable unitary state income tax returns. For financial reporting purposes, the provision for income taxes through August 11 of the first quarter of fiscal year 1995 was calculated as if the Company filed separate federal and state income tax returns.

Minority interests

Minority interests represent the proportionate equity interest of other partners and stockholders in the Company's consolidated entities which are not wholly owned. As of December 31, 1997, these included 29 active partnerships and corporations.

Stock-based compensation

During the year ended December 31, 1996, the Company adopted Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation ("SFAS 123"). This pronouncement requires the Company to elect to account for stock-based compensation on a fair value based model or an intrinsic value based model. The intrinsic value based model is currently used by the Company and is the accounting principle prescribed by Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees ("APB 25"). Under this model, compensation cost is the excess, if any, of the quoted market price of the stock at the date of grant or other measurement date over the amount an employee must pay to acquire the stock. The fair value based model prescribed by SFAS 123 requires the Company to value stock-based compensation using an accepted valuation model. Compensation cost is measured at the grant date based on the value of the award and would be recognized over the service period which is usually the vesting period. SFAS 123 requires the Company to either reflect the results of the valuation in the consolidated financial statements or alternatively continue to apply the provisions of APB 25 and make appropriate disclosure of the impact of such valuation in the accompanying notes to consolidated financial statements.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

The Company has elected to continue to apply the provisions of APB 25 to their employee stock-based compensation plans and therefore has included the required disclosure of the pro forma impact on net income and earnings per share of the difference between compensation expense using the intrinsic value method and the fair value method (see Note 10).

Earnings per share and unaudited pro forma net income per share

In February 1997, the Financial Accounting Standards Board issued the Statement of Financial Accounting Standards No. 128, Earnings Per Share ("SFAS 128"). The Company adopted SFAS 128 in the fourth quarter of 1997, as required by this pronouncement. SFAS 128 establishes standards for computing and presenting earnings per share. Basic earnings per share is calculated by dividing net income before extraordinary items and net income by the weighted average number of shares of common stock outstanding. Accordingly, earnings per common share--assuming dilution includes the dilutive effects of stock options and warrants using the treasury stock method, in determining the weighted average number of shares of common stock outstanding. Earnings per share for all periods presented have been restated following the provisions of SFAS 128.

Interest rate swap agreements

The Company has entered into two interest rate swap agreements (see Note 8) as a means of managing its interest rate exposure. The Company has not entered these agreements for trading or speculative purposes. These agreements have the effect of converting the Company's line of credit obligation from a variable rate to a fixed rate. Net amounts paid or received are reflected as adjustments to interest expense. The counterparty to these agreements is a large international financial institution. These interest rate swap agreements subject the Company to financial risk that will vary during the life of the agreements in relation to the prevailing market interest rates. The Company is also exposed to credit loss in the event of non-performance by this counterparty. However, the Company does not anticipate non-performance by the other party, and no material loss is expected from non-performance by the counterparty.

Financial instruments

The Company's financial instruments consist primarily of cash, accounts receivable, notes receivable from related parties, accounts payable, employee compensation and benefits, and other accrued liabilities. These balances, as presented in the financial statements at December 31, 1996 and 1997, approximate their fair value. Borrowings under the Company's two credit facilities, of which \$353,000,000 was outstanding as of December 31, 1997, reflect fair value as they are subject to fees and rates competitively determined in the marketplace. The fair value of the interest rate swap agreements are based on the present value of expected future cash flows from the agreement and was in a net payable position of \$49,000 at December 31, 1997.

Use of estimates

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

Unaudited financial statements

In December 1995, the Company changed its year-end to December 31 from May 31. The information presented for the seven months ended December 31, 1994 and the year ended December 31, 1995 has not been



## TOTAL RENAL CARE HOLDINGS, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

audited. In the opinion of management, the unaudited consolidated statements of income and of cash flows include all adjustments consisting solely of normal recurring adjustments necessary to present fairly the Company's consolidated results of operations and cash flows for the seven months ended December 31, 1994 and the year ended December 31, 1995.

## Reclassifications

Certain prior year balances have been reclassified to conform to the current year presentation.

## 2. PROPERTY AND EQUIPMENT

Property and equipment comprise the following:

	DECEMBER 31,	
	1996	1997
Land.....	\$ 373,000	\$ 448,000
Buildings.....	3,978,000	4,275,000
Leaseholds and improvements.....	25,463,000	49,089,000
Equipment.....	50,174,000	77,816,000
Construction in progress.....	4,638,000	7,352,000
	84,626,000	138,980,000
Less accumulated depreciation and amortization...	(26,360,000)	(38,919,000)
	\$58,266,000	\$100,061,000
	=====	=====

Depreciation and amortization expense on property and equipment was \$3,163,000, \$2,326,000, \$7,302,000 and \$12,427,000 for the year ended May 31, 1995, the seven months ended December 31, 1995, and the years ended December 31, 1996 and 1997, respectively.

## 3. INTANGIBLE ASSETS

A summary of intangible assets is as follows:

	DECEMBER 31,	
	1996	1997
Goodwill.....	\$152,122,000	\$333,680,000
Patient lists.....	12,765,000	22,420,000
Noncompetition agreements.....	22,978,000	39,156,000
Deferred debt issuance costs.....	4,488,000	18,037,000
Other.....	1,108,000	2,469,000
	193,461,000	415,762,000
Less accumulated amortization.....	(12,844,000)	(26,025,000)
	\$180,617,000	\$389,737,000
	=====	=====

Amortization expense applicable to intangible assets was \$1,577,000, \$2,057,000, \$8,066,000, and \$14,697,000 for the year ended May 31, 1995, the seven months ended December 31, 1995, and the years ended December 31, 1996 and 1997, respectively.

## TOTAL RENAL CARE HOLDINGS, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

## 4. PREPAID EXPENSES AND OTHER CURRENT ASSETS

Prepaid expenses and other current assets comprise the following:

	DECEMBER 31,	
	1996	1997
Supplier rebates and other non-trade receivables...	\$ 6,424,000	\$ 9,664,000
Prepaid income taxes.....	2,708,000	649,000
Prepaid expenses.....	1,504,000	2,259,000
Deposits.....	135,000	174,000
	\$10,771,000	\$12,746,000
	=====	=====

## 5. NOTES RECEIVABLE FROM RELATED PARTIES

During the year ended December 31, 1997 the Company entered into various agreements to provide funding for expansion to certain companies that provide renal dialysis or renal related services. These notes receivables are secured by the assets and operations of these companies. Approximately \$9,205,000 was outstanding and included in notes receivable from related parties at December 31, 1997. Additionally, a note receivable from the Company's President was approximately \$1,678,000 and \$1,820,000 at December 31, 1996 and 1997, respectively.

## 6. OTHER ACCRUED LIABILITIES

Other accrued liabilities comprise the following:

	DECEMBER 31,	
	1996	1997
Customer refunds.....	\$6,068,000	\$4,608,000
Other.....	1,677,000	2,613,000
	\$7,745,000	\$7,221,000
	=====	=====

## 7. INCOME TAXES

The provision for income taxes consists of the following:

	YEAR ENDED MAY 31, 1995	SEVEN MONTHS ENDED DECEMBER 31, 1995	YEARS ENDED DECEMBER 31, 1996	1997
Current				
Federal.....	\$3,275,000	\$3,708,000	\$12,803,000	\$21,518,000
State.....	952,000	954,000	2,881,000	4,304,000
Deferred				
Federal.....	(555,000)	9,000	544,000	(567,000)
State.....	(161,000)	(40,000)	123,000	(114,000)
	\$3,511,000	\$4,631,000	\$16,351,000	\$25,141,000
	=====	=====	=====	=====

## TOTAL RENAL CARE HOLDINGS, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

Temporary differences which give rise to deferred tax assets and liabilities are as follows:

	DECEMBER 31,	
	1996	1997
Receivables, primarily allowance for doubtful accounts.....	\$ 2,724,000	\$ 4,446,000
Accrued vacation.....	831,000	1,717,000
Deferred compensation.....	107,000	67,000
Gross deferred tax assets.....	3,662,000	6,230,000
Depreciation and amortization.....	(1,811,000)	(2,454,000)
Intangible assets.....	(1,173,000)	(2,713,000)
Change in tax accounting method.....	(313,000)	(17,000)
Gross deferred tax liabilities.....	(3,297,000)	(5,184,000)
Net deferred tax assets.....	\$ 365,000	\$ 1,046,000
	=====	=====

The reconciliation between the Company's effective tax rate and the U.S. federal income tax rate on income is as follows:

	YEAR ENDED MAY 31, 1995	SEVEN MONTHS ENDED DECEMBER 31, 1995	YEAR ENDED DECEMBER 31, ----- 1996 1997	
Federal income tax rate.....	34.0%	35.0%	35.0%	35.0%
State taxes, net of federal benefit..	5.9%	5.3%	4.7%	4.5%
Nondeductible amortization of intangible assets.....	1.1%	1.1%	0.8%	0.6%
Other.....	0.2%	0.1%	0.1%	0.1%
Effective tax rate.....	41.2%	41.5%	40.6%	40.2%
Minority interests in partnerships...	(5.9%)	(5.5%)	(3.1%)	(2.5%)
Effective tax rate before minority interests.....	35.3%	36.0%	37.5%	37.7%
	====	====	====	====

## 8. LONG-TERM DEBT

Long-term debt comprises:

	DECEMBER 31,	
	1996	1997
Credit facilities.....	\$ 85,000,000	\$353,000,000
Acquisition obligations.....	15,886,000	2,183,000
Capital lease obligations (see Note 9).....	3,122,000	2,509,000
Other.....	608,000	892,000
	104,616,000	358,584,000
Less current portion.....	(2,064,000)	(2,021,000)
	\$102,552,000	\$356,563,000
	=====	=====

TOTAL RENAL CARE HOLDINGS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

Maturities of long-term debt for the years ending December 31 are as follows:

1998.....	\$ 2,021,000
1999.....	1,995,000
2000.....	612,000
2001.....	290,000
2002.....	88,000
Thereafter.....	353,578,000

12% Senior Subordinated Discount Notes

In August 1994, the Company completed a public offering consisting of units of 12% Senior Subordinated Discount Notes (the "Notes") and common stock. Aggregate proceeds from the offering were \$71,294,000, of which \$900,000 was allocated to the common stock, based upon the estimated value of the stock, and the remaining \$70,394,000 to the Notes. The Notes had a stated maturity of August 15, 2004 with the first semi-annual cash interest payment commencing on February 15, 1998, at a rate of 12% per annum. Prior to February 15, 1998, interest was paid in kind through amortization of the discount. The discount was amortized using the effective interest rate of 12.39%.

On December 7, 1995, the Company redeemed 35% of the accreted value of the Notes equaling \$28,749,000 at a redemption premium of 111% for a total redemption price of \$31,912,000. An extraordinary loss on the early extinguishment of debt of \$4,258,000, net of income tax effect of \$1,703,000, was recorded during the seven months ended December 31, 1995. In July and September 1996, the Company retired the remaining 65% of the outstanding Notes for \$68,499,000, including consent payments of \$1,100,000. An extraordinary loss on the early extinguishment of debt of \$12,623,000, net of income tax effect of \$4,923,000, was recorded in the year ended December 31, 1996.

Credit Facilities

On October 24, 1997, the Company expanded its existing \$400 million revolving credit facility to an aggregate of \$1,050,000,000 consisting of a seven-year \$800 million revolving credit facility and a ten-year \$250 million term facility. Under the \$800 million revolving credit facility, up to \$100,000,000 may be used in connection with letters of credit, and up to \$15,000,000 in short-term funds may be borrowed the same day notice is given to the banks under a "Swing Line" facility. Up to \$75,000,000 of the available letters of credit or borrowings under the revolving senior credit facility may be utilized for foreign financing. In general, borrowings under the credit facilities bear interest at one of two floating rates selected by the Company: (i) the Alternate Base Rate (defined as the higher of The Bank of New York's prime rate or the federal funds rate plus 0.5%); or (ii) Adjusted LIBOR (defined as the 30-, 60-, 90- or 180-day London Interbank Offered Rate, adjusted for statutory reserves) plus a margin that ranges from 0.45% to 1.75% depending on the Company's leverage ratio. Swing Line borrowings bear interest at either a rate negotiated by the Company and the banks at the time of borrowing or, if no rate is negotiated and agreed upon, the Alternate Base Rate.

Maximum borrowings under the \$800 million revolving credit facility will be reduced by \$75,000,000 on September 30, 2001, \$125,000,000 on September 30, 2002, and another \$200,000,000 on September 30, 2003, and the revolving credit facility terminates on September 30, 2004. Under the \$250 million term facility, payments of \$2,500,000 shall be made each consecutive year beginning on September 30, 1998 and continuing through September 30, 2006. The remaining balance of \$227,500,000 is due on September 30, 2007 when the term facility terminates. The credit facilities contain financial and operating covenants including, among other things, requirements that the Company maintain certain financial ratios and satisfy certain financial tests, and imposes limitations on the Company's ability to make capital expenditures, to incur other indebtedness and to pay dividends. The Company is in compliance with all such covenants.

TOTAL RENAL CARE HOLDINGS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

The Company and certain of its subsidiaries, including Total Renal Care, Inc. ("TRC"), TRC West, Inc., Total Renal Care Acquisition Corp., RTC, Renal Treatment Centers--Mid-Atlantic, Inc., Renal Treatment Centers--Northeast, Inc., Renal Treatment Centers--California, Inc., Renal Treatment Centers--West, Inc. and Renal Treatment Centers--Southeast, Inc. (see Note 17), have guaranteed the Company's obligations under the credit facilities on a senior basis.

Acquisition Obligations

In conjunction with certain facility acquisitions, the Company issued three letters of credit. Two of these were released on April 1, 1997. The remaining letter of credit of \$3,000,000 is being released to the seller in three annual principal installments of \$1,000,000 commencing January 1997. The Company has also agreed to pay the seller interest at 6.5% on the outstanding principal. As of December 31, 1996 and 1997 the aggregate amount outstanding, including accrued interest, was \$15,886,000 and \$2,183,000, respectively.

Interest Rate Swap Agreements

On November 25, 1996, the Company entered into a seven-year interest rate swap agreement involving the exchange of fixed and floating interest payment obligations without the exchange of the underlying principal amounts. At December 31, 1997 the total notional principal amount of this interest rate swap agreement was \$100,000,000 and the effective interest rate thereon was 7.57%.

On July 24, 1997, the Company entered into a ten-year interest rate swap agreement. At December 31, 1997 the total notional principal amount of this interest rate swap agreement was \$200,000,000 and the effective interest rate thereon was 7.77%.

9. LEASES

The Company leases the majority of its facilities under noncancelable operating leases expiring in various years through 2021. Most lease agreements cover periods from five to ten years and contain renewal options of five to ten years at the fair rental value at the time of renewal or at rates subject to consumer price index increases since the inception of the lease. In the normal course of business, operating leases are generally renewed or replaced by other similar leases.

Future minimum lease payments under noncancelable operating leases for the years ending December 31 are as follows:

1998.....	\$14,808,000
1999.....	13,000,000
2000.....	11,890,000
2001.....	9,626,000
2002.....	8,774,000
Thereafter.....	39,969,000
	-----
Total minimum lease payments.....	\$98,067,000
	=====

Rental expense under all operating leases for the year ended May 31, 1995, the seven months ended December 31, 1995 and the years ended December 31, 1996 and 1997 amounted to \$3,323,000, \$2,644,000, \$9,054,000 and \$14,599,000, respectively.

TOTAL RENAL CARE HOLDINGS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

The Company also leases certain equipment under capital lease agreements. Future minimum lease payments under capital leases for the years ending December 31 are as follows:

1998.....	\$ 978,000
1999.....	906,000
2000.....	564,000
2001.....	245,000
2002.....	28,000
Thereafter.....	176,000
	-----
	2,897,000
Less--Portion representing interest.....	388,000
	-----
Total capital lease obligation, including current portion of \$782,000.....	\$2,509,000
	=====

The net book value of fixed assets under capital lease was \$1,858,000 and \$2,228,399 at December 31, 1996 and 1997, respectively. Capital lease obligations are included in long-term debt (see Note 8).

#### 10. STOCKHOLDERS' EQUITY

##### Public offerings of common stock

On November 3, 1995, the Company completed an initial public offering of its common stock at an offering price of \$9.30 per share. The Company received net proceeds of \$98,294,000 after the deduction of underwriting discounts and commissions and other expenses. The Company used net proceeds of \$62,912,000 to redeem outstanding notes and to repay outstanding borrowings. The remainder of the net proceeds was used for general corporate purposes, acquisitions, de novo facility developments and other capital expenditures.

On April 3, 1996, and October 31, 1996 the Company completed equity offerings of its 13,416,667 and 4,166,667 shares of common stock, respectively; 5,833,333 and 833,334, respectively, of which were sold for the Company's account and 7,583,333 and 3,333,333 respectively, of which were sold by certain of the Company's stockholders. The net proceeds received by the Company of \$109,968,000 and \$18,350,000, respectively, were used to repay borrowings incurred under the Company's credit facilities in connection with acquisitions, to repurchase and subsequently retire its 12% senior subordinated debt, to finance other acquisitions and de novo developments and for working capital and other corporate purposes.

##### Change in shares, stock splits and dividends

In July 1994, the Company's Certificate of Incorporation was amended to increase the number of authorized shares of common stock from 1,000 shares to 35,000,000 shares and to reduce the par value of such stock from \$1.00 per share to \$0.001 per share. Concurrent with this change, the Board of Directors approved a 1,000-for-1 stock split. Shares held by Tenet were the only shares affected by this action. Following the split, Tenet purchased an additional 4,888,890 shares of common stock for \$4,400.

Immediately following the public offering of 12% senior subordinated debt in August 1994, the Company paid Tenet a dividend totaling \$81,652,000. The dividend comprised \$75,500,000 in cash and \$6,152,000 in the forgiveness of Tenet's intercompany balance due the Company. Subsequently, the Company has not made, nor does it intend to make, dividends to its stockholders.

During October 1995 the Company's directors authorized an increase in the authorized number of shares of common stock to 55,000,000, authorized 5,000,000 new shares of \$0.001 par value preferred stock, and approved

## TOTAL RENAL CARE HOLDINGS, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

a three-into-two reverse stock split of the Company's common stock. All information in these consolidated financial statements pertaining to shares of common stock and per share amounts have been restated to retroactively reflect the stock splits.

On September 30, 1997 the Company announced a common stock dividend to all stockholders of record as of October 7, 1997, to be effective on October 20, 1997. Each stockholder received two additional shares of common stock for each three shares held. Fractional shares calculated as a result of the stock dividend were paid out in cash in the amount of approximately \$14,000. As such, all share and per share amounts presented in the financial statements and related notes thereto have been retroactively restated to reflect this dividend which was accounted for as a stock split.

## Earnings per share

The reconciliation of the numerators and denominators used to calculate earnings per share for all periods presented is as follows:

		SEVEN MONTHS ENDED		YEAR ENDED		
	YEAR ENDED MAY 31, 1995	DECEMBER 31, 1994	DECEMBER 31, 1995	DECEMBER 31, 1995	DECEMBER 31, 1996	DECEMBER 31, 1997
		(UNAUDITED)		(UNAUDITED)		
Net income:						
As reported.....	\$4,852,000	\$2,650,000	\$3,912,000	\$6,114,000	\$16,025,000	\$36,977,000
	=====	=====	=====	=====	=====	=====
Applicable common shares:						
Average outstanding during the period.....	18,125,000	14,822,000	27,728,000	24,864,000	41,825,000	44,429,000
Average mandatorily redeemable common shares outstanding during the period.....	110,000					
Reduction in shares in connection with notes receivable from employees.....	(185,000)	(130,000)	(128,000)	(122,000)	(130,000)	(125,000)
	-----	-----	-----	-----	-----	-----
Weighted average number of shares outstanding for use in computing earnings per share.....	18,050,000	14,692,000	27,600,000	24,742,000	41,695,000	44,304,000
Outstanding stock options (based on the treasury stock method).....	1,784,000	1,764,000	2,107,000	2,170,000	1,293,000	998,000
	-----	-----	-----	-----	-----	-----
Adjusted weighted average number of common and common share equivalent shares outstanding..	19,834,000	16,456,000	29,707,000	26,912,000	42,988,000	45,302,000
	=====	=====	=====	=====	=====	=====
Earnings per common share.....	\$0.27	\$0.18	\$0.14	\$0.25	\$0.38	\$0.83
Earnings per common share-- assuming dilution.....	\$0.24	\$0.16	\$0.13	\$0.23	\$0.37	\$0.82

Stock-Based Compensation Plans

At December 31, 1997, the Company has four stock-based compensation plans, which are described below.

1994 Stock Plan. In August 1994, the Company established the Total Renal Care Holdings, Inc. 1994 Equity Compensation Plan ("1994 Stock Plan") which provides for awards of nonqualified stock options to purchase common stock and other rights to purchase shares of common stock to certain employees, directors, consultants and facility medical directors of the Company.

Under terms of the 1994 Stock Plan, the Company may grant awards for up to 8,474,078 shares of common stock. Original options granted generally vest on the ninth anniversary of the date of grant, subject to accelerated vesting in the event the Company meets certain performance criteria. In April 1996, the Company changed the vesting schedule for new options granted so that options vest over four years from the date of grant. The exercise price of each option equals the market price of the Company's stock on the date of grant, and an option's maximum term is ten years.

Purchase rights to acquire 1,314,450 common shares for \$.90-\$3.60 per share were awarded to certain employees under the 1994 Stock Plan, the majority of which were granted in connection with the change in control. All such rights were exercised and the Company received notes for the uncollected portion of the purchase proceeds. The notes bear interest at the lesser of The Bank of New York's prime rate or 8%, are full recourse to the employees, and are secured by the employees' stock. The notes are repayable four years from the date of issuance, subject to certain prepayment requirements. At December 31, 1995, 1996 and 1997 the outstanding notes plus accrued interest totaled \$378,000, \$227,000, and \$212,000 respectively.

During the year ended May 31, 1995, 1,477,778 options to purchase common stock were issued to the Company's President. These options originally vested 50% over four years and 50% in the same manner as other options granted under the 1994 Stock Plan. In September 1995, the Board of Directors and stockholders agreed to accelerate the President's vesting period and all of the options became 100% vested. Pursuant to this action, the President exercised all of the stock options through issuance of a full recourse note of \$1,330,000 bearing interest at the lesser of prime or 8%. Additionally, the President executed a full recourse note for \$1,349,000 bearing interest at the lesser of prime or 8% per annum to meet his tax liability in connection with the stock option exercise. In April 1996, this note was increased by an additional \$173,000. These notes are secured by other shares of company stock and mature in September 1999 or upon disposition of the common stock by the President.

1995 Stock Plan. In November 1995, the Company established the Total Renal Care Holdings, Inc. 1995 Equity Incentive Plan ("1995 Stock Plan") which provides awards of stock options and the issuance of common shares subject to certain restrictions to certain employees, directors and other individuals providing services to the Company. There are 1,666,667 common shares reserved for issuance under the 1995 Stock Plan. Options granted generally vest over four years from the date of grant and an option's maximum term is ten years, subject to certain restrictions. The Company generally issues awards with the exercise prices equal to the market price of the Company's stock on the date of grant.

1997 Stock Plan. In July 1997, the Company established the Total Renal Care Holdings, Inc. 1997 Equity Compensation Plan ("1997 Stock Plan") which provides awards of stock options and the issuance of common shares subject to certain restrictions to certain employees, directors and other individuals providing services to the Company. There are 4,166,667 common shares reserved for issuance under the 1997 Stock Plan. Options granted generally vest over four years from the date of grant and an option's maximum term is ten years. The Company generally issues awards with the exercise prices equal to the market price of the Company's stock on the date of grant.



## TOTAL RENAL CARE HOLDINGS, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions used for grants for the seven months ended December 31, 1995, year ended December 31, 1996, and year ended December 31, 1997, respectively: dividend yield of 0 percent for all periods; weighted average expected volatility of 40.5%, 36.35% and 35.12%; risk-free interest rates of 5.92%, 6.56% and 6.40% and expected lives of six years for all periods.

A combined summary of the status of the 1994 Stock Plan, 1995 Stock Plan, and 1997 Stock Plan as of and for the seven months ended December 31, 1995 and years ended December 31, 1996 and 1997, is presented below:

	SEVEN MONTHS ENDED DECEMBER 31, 1995		YEAR ENDED DECEMBER 31, 1996		YEAR ENDED DECEMBER 31, 1997	
	OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE	OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE	OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE
Outstanding at beginning of period.....	2,863,890	\$0.90	1,441,685	\$ 1.91	3,118,394	\$13.82
Granted.....	322,238	5.41	1,818,913	22.28	3,931,080	19.74
Exercised.....	(1,744,443)	0.90	(111,647)	0.92	(275,620)	3.96
Forfeited.....			(30,557)	2.43	(1,734,016)	22.46
	-----	-----	-----	-----	-----	-----
Outstanding at end of year.....	1,441,685	\$1.91	3,118,394	\$13.82	5,039,838	\$16.01
	=====	=====	=====	=====	=====	=====
Options exercisable at year end.....	351,855		663,007		797,474	
Weighted-average fair value of options granted during the year.....	\$ 3.17		\$ 10.52		\$ 9.15	

Forfeitures and grants include the effects of modifications to the terms of awards as if the original award was repurchased and exchanged for a new award of greater value. On April 24, 1997, 1,649,735 shares were cancelled and reawarded at the market price as of that date. The new awards vest annually over 3 years on the anniversary date of the new award.

The following table summarizes information about fixed stock options outstanding at December 31, 1997:

RANGE OF EXERCISE PRICES	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
	OPTIONS	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED-AVERAGE EXERCISE PRICE	OPTIONS	WEIGHTED-AVERAGE EXERCISE PRICE
\$ 0.01-\$ 5.00	950,917	6.8 years	\$ 1.15	666,411	\$1.08
\$ 5.01-\$10.00	19,735	7.0 years	5.44	10,531	5.47
\$10.01-\$15.00	13,890	7.8 years	11.82	7,230	11.82
\$15.01-\$20.00	3,561,952	8.8 years	18.64	99,969	17.49
\$20.01-\$25.00	100,002	9.3 years	22.07	2,083	20.73
\$25.01-\$30.00	300,283	9.6 years	26.20	11,250	28.43
\$30.01-\$35.00	93,059	9.8 years	30.79		
	-----	-----	-----	-----	-----
\$ 0.01-\$35.00	5,039,838	8.5 years	\$16.01	797,474	\$3.73
	=====	=====	=====	=====	=====

Stock Purchase Plan. In November 1995, the Company established the Total Renal Care Holdings, Inc. Employees Stock Purchase Plan (the "Stock Purchase Plan") which entitles qualifying employees to purchase up to \$25,000 of common stock during each calendar year. The amounts used to purchase stock are typically accumulated through payroll withholdings and through an optional lump sum payment made in advance of the first day of the purchase right period. The Stock Purchase Plan allows employees to purchase stock for the lesser of 100% of the fair market value on the first day of the purchase right period or 85% of the fair market value on the last day of the purchase right period. Except for the initial purchase right period, which began on

## TOTAL RENAL CARE HOLDINGS, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

November 3, 1995 (the date of completion of the initial public offering, and ended on December 31, 1996), each purchase right period begins on January 1 or July 1, as selected by the employee and ends on December 31. Payroll withholdings related to the Stock Purchase Plan, included in accrued employee compensation and benefits, were \$1,790,000 and \$1,120,307 at December 31, 1996 and 1997 respectively. Subsequent to December 31, 1996 and December 31, 1997, 174,775 and 49,060 shares, respectively were issued to satisfy the Company's obligations under the Plan.

For the November 1995 and July 1996 purchase right periods the fair value of the employees' purchase rights were estimated on the beginning date of the purchase right period using the Black-Scholes model with the following assumptions for grants on November 3, 1995 and July 1, 1996, respectively: dividend yield of 0 percent for both periods; expected volatility of 36.6 percent for both periods; risk-free interest rate of 5.5 and 6.6 percent and expected lives of 1.2 and 0.5 years. Using these assumptions, the weighted-average fair value of purchase rights granted on November 3, 1995 and July 1, 1996 is \$2.86 and \$7.37, respectively.

The fair value of the January 1, 1997 and July 1, 1997 purchase right period were not estimated at December 31, 1997 because of the employee's ability to withdraw from participation through December 31.

Pro forma net income and earnings per share. The Company applied APB 25 and related interpretations in accounting for all of its plans. Accordingly, no compensation cost has been recognized for its fixed stock option plans and its stock purchase plan. Had compensation cost for the Company's stock-based compensation plans been determined consistent with SFAS 123, the Company's net income and earnings per share would have been reduced to the pro forma amounts indicated below:

	SEVEN MONTHS ENDED DECEMBER 31, 1995	YEAR ENDED DECEMBER 31, 1996	YEAR ENDED DECEMBER 31, 1997
Income before extraordinary item.....	\$6,159,000	\$20,480,000	\$32,210,000
Extraordinary loss related to early extinguishment of debt, net of tax.....	2,555,000	7,700,000	-----
Net income.....	\$3,604,000	\$12,780,000	\$32,210,000
	=====	=====	=====
Earnings per common share:			
Income before extraordinary item....	\$ 0.22	\$ 0.49	\$ 0.73
Extraordinary loss.....	(0.09)	(0.18)	-----
Net income.....	\$ 0.13	\$ 0.31	\$ 0.73
	=====	=====	=====
Weighted average number of common shares outstanding.....	27,600,000	41,695,000	44,304,000
	=====	=====	=====
Earnings per common share-assuming dilution:			
Income before extraordinary item....	\$ 0.22	\$ 0.49	\$ 0.73
Extraordinary loss.....	(0.09)	( 0.18)	-----
Net income.....	\$ 0.13	\$ 0.31	\$ 0.73
	=====	=====	=====
Weighted average number of common shares and equivalents outstanding-- assuming dilution.....	28,167,000	41,695,000	44,304,000
	=====	=====	=====

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

## Stock issued to employees outside of plans

In connection with the change in control, the Company awarded its Chief Executive Officer and Chief Operating Officer rights to purchase 1,855,555 and 222,222 common shares, respectively, at a purchase price of \$.90 per share. These rights were awarded outside of the 1994 Stock Plan in connection with the respective employment agreements. All such purchase rights were made and the Company received notes totaling \$935,000 for the uncollected portion of the purchase proceeds. The notes bear terms similar to those issued in connection with the 1994 Stock Plan.

## 11. TRANSACTIONS WITH RELATED PARTIES

The Company provides dialysis services to Tenet hospital patients under agreements with terms of one to three years. The contract terms are comparable to contracts with unrelated third parties. Included in the receivable from Tenet are amounts related to these services of \$347,000 and \$534,000 at December 31, 1996 and 1997, respectively. Net operating revenues received from Tenet for these services were \$2,130,000, \$1,332,000, \$2,260,000 and \$2,640,000 for the year ended May 31, 1995, the seven months ended December 31, 1995, and the years ended December 31, 1996 and 1997, respectively.

Prior to October 1994, company employees were eligible to participate in the Tenet Retirement Savings Plan, a defined contribution retirement plan, covering substantially all full-time employees, whereby employees' contributions to the plan were matched by the Company up to certain limits. Defined contributions made by the Company for the year ended May 31, 1995 amounted to \$152,000.

Prior to December 1994, the Company was insured for employee health coverage and a substantial portion of workers' compensation through self-insurance programs administered by Tenet. Additionally, all professional and general liability risks were insured by a wholly owned subsidiary of Tenet. The Company has no liability for employee health coverage claims incurred prior to December 31, 1994 or workers' compensation claims prior to August 11, 1994. Insurance expense under these programs amounted to \$1,409,000 for year ended May 31, 1995.

## DLJMB

An affiliate of DLJMB was the underwriter for a public debt offering of units, comprising 12% Senior Subordinated Discount Notes and common stock, and DLJMB participated in the change in control transaction in which DLJMB and certain employees acquired 74% of the Company. Fees for these transactions were \$2,496,000 and \$1,160,000, respectively. During the seven months ended December 31, 1995 and the year ended December 31, 1996 an affiliate of DLJMB also was one of several underwriters for the initial public offering of common stock as well as the two additional public stock offerings in which the Company issued 11,500,000, 11,666,667 and 833,334 shares, respectively. Fees for these transactions to DLJMB or its affiliates were \$7,245,000, \$5,075,000, and \$780,000, respectively.

On August 12, 1997, the Company filed a registration statement with the Securities and Exchange Commission for an offering of 4,325,873 shares of common stock to be offered by affiliates of DLJ Merchant Banking Partners, L.P. ("DLJMB"), as well as certain officers of the Company. Of the shares sold, 3,673,723 were offered by DLJ Merchant Banking affiliates, representing their entire remaining interest in the Company. Donaldson, Lufkin & Jenrette Securities Corporation was the sole underwriter of the offering. The Company did not receive any of the proceeds from the sale of shares being sold by the selling stockholders. Effective with the August 1997 public offering of common stock, DLJMB and its affiliates are no longer considered a related party.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

## 12. EMPLOYEE BENEFIT PLAN

The Company has a savings plan (the "Plan") for substantially all employees, which has been established pursuant to the provisions of Section 401(k) of the Internal Revenue Code ("IRC"). The Plan provides for employees to contribute from 1% to 15% of their base annual salaries on a tax-deferred basis not to exceed IRC limitations. The Company, in its sole discretion, may make a contribution under the Plan each fiscal year as determined by the Board of Directors. This contribution was allocated for the year ended May 31, 1995 to each participant not eligible for participation in the 1994 Stock Plan (see Note 10) in proportion to the compensation paid during the year and the length of employment for each of the participants. For the year ended May 31, 1995, the Company accrued contributions under the Plan in the amount of \$200,000. The Company did not make any contributions subsequent to May 31, 1995.

## 13. CONTINGENCIES

The Company's laboratory subsidiary is presently the subject of a Medicare carrier review. The carrier has requested certain medical and billing records for certain patients and the Company has provided the requested records. The carrier has not informed the Company of the reason for or the exact nature or scope of this review.

The Company is subject to various claims and lawsuits in the ordinary course of business. In the opinion of management, the ultimate resolution of these matters will not have a material adverse effect on the Company's financial condition, results of operations or cash flows.

## 14. ACQUISITIONS

Beginning in August 1994, the Company implemented an acquisition strategy which through December 31, 1997 has resulted in the acquisition of 135 facilities providing services to ESRD patients, 99 programs providing acute hospital in-patient dialysis services, two laboratories, a vascular access management company and a clinical research company specializing in renal and renal related services. In addition, during this period the Company developed 25 de novo facilities, entered into a management contract covering an additional two unaffiliated facilities and purchased the minority interest at one of its existing facilities. The following is a summary of acquisitions activity:

	YEAR ENDED MAY 31, 1995	SEVEN MONTHS ENDED DECEMBER 31, 1995	YEAR ENDED DECEMBER 31, ----- 1996                      1997	
Number of facilities acquired.....	15	12	57	51
Number of common shares issued.....	495,773	1,238,033	102,645	17,613
Numbers of mandatorily redeemable shares issued...	1,136,112			
Number of common stock options issued.....		66,667		
Estimated fair value of common shares issued.....	\$ 446,000	\$ 5,284,000	\$ 1,830,000	\$ 273,000
Estimated fair value of mandatorily redeemable shares issued.....	3,990,000			
Estimated fair value of common stock options issued.....		51,000		
Payable to former owners of acquired facility.....		1,243,000		
Acquisition obligations (see Note 8).....			15,886,000	
Cash paid.....	23,007,000	28,303,000	138,202,000	200,624,000
Aggregate purchase price....	\$27,443,000	\$34,881,000	\$155,918,000	\$200,897,000
	=====	=====	=====	=====

## TOTAL RENAL CARE HOLDINGS, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

All of the acquisitions were accounted for as purchases and, accordingly, the assets and liabilities of the acquired entities were recorded at their estimated fair market values at the dates of acquisition. The initial allocations of fair market value are preliminary and subject to adjustment during the first year following the acquisition. The results of operations of the facilities and laboratories have been included in the Company's financial statements from their respective acquisition dates. These initial allocations were as follows:

	YEAR ENDED MAY 31, 1995	SEVEN MONTHS ENDED DECEMBER 31, 1995	YEARS ENDED DECEMBER 31, ----- 1996	1997
Identified intangibles....	\$ 4,807,000	\$ 8,063,000	\$ 20,695,000	\$ 25,570,000
Goodwill.....	18,782,000	24,700,000	102,608,000	170,477,000
Tangible assets.....	6,845,000	6,798,000	41,100,000	19,859,000
Liabilities assumed.....	(2,991,000)	(4,680,000)	(8,485,000)	(15,009,000)
	-----	-----	-----	-----
Total purchase price....	\$27,443,000	\$34,881,000	\$155,918,000	\$200,897,000
	=====	=====	=====	=====

The following summary, prepared on a pro forma basis, combines the results of operations as if the acquisitions had been consummated as of the beginning of each of the periods presented, after including the impact of certain adjustments such as amortization of intangibles, interest expense on acquisition financing and income tax effects.

	YEAR ENDED DECEMBER 31, 1996 (UNAUDITED)	YEAR ENDED DECEMBER 31, 1997 (UNAUDITED)
Net revenues.....	\$401,541,000	\$520,092,000
Net income before extraordinary items.....	\$ 17,000,000	\$ 39,810,000
Pro forma net income per share before extraordinary items.....	\$ 0.59	\$ 0.90
Pro forma net income per share before extraordinary items--assuming dilution.....	\$ 0.57	\$ 0.88

The unaudited pro forma results are not necessarily indicative of what actually would have occurred if the acquisitions had been completed prior to the beginning of the periods presented. In addition, they are not intended to be a projection of future results and do not reflect any of the synergies, additional revenue-generating services or direct facility operating expense reduction that might be achieved from combined operations.

Subsequent to December 31, 1997, the Company entered into 13 agreements to acquire additional facilities of which seven have been consummated and six are expected to close imminently. The aggregate purchase price is approximately \$140 million. The composition of the final purchase price is expected to be cash and proceeds from the Company's credit facilities, however, a portion of the purchase price may consist of issuance of the Company's common stock. The Company is actively pursuing additional acquisitions on which letters of intent had not been signed as of the date of these financial statements.

Additionally, as described in Note 17, subsequent to December 31, 1997, the Company merged with another provider of dialysis services.

## TOTAL RENAL CARE HOLDINGS, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

## 15. SUPPLEMENTAL CASH FLOW INFORMATION

The table below provides supplemental cash flow information:

	YEAR ENDED MAY 31, 1995	SEVEN MONTHS ENDED DECEMBER 31, 1995	YEAR ENDED DECEMBER 31, 1996	YEAR ENDED DECEMBER 31, 1997
Cash paid for:				
Income taxes.....	\$4,112,000	\$ 957,000	\$12,871,000	\$20,364,000
Interest, net of capitalized interest.....	256,000	1,063,000	2,120,000	13,511,000
Noncash investing and financing activities:				
Notes receivable for issuance of common stock.....	1,508,000	1,330,000		
Dividend of Tenet intercompany receivable.....	6,152,000			
Estimated value of stock and options issued in acquisitions.....	4,436,000	5,335,000	2,810,000	273,000
Fixed assets acquired under capital lease obligations...		1,483,000	1,117,000	530,000
Contribution to partnerships.....		1,111,000	430,000	2,318,000

## 16. SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

Summary unaudited quarterly financial data for the years ended December 31, 1996 and 1997 from the Company's filings on Form 10-Q is as follows (in thousands, except per share amounts):

	MARCH 31, 1996	JUNE 30, 1996	SEPTEMBER 30, 1996	DECEMBER 31, 1996	MARCH 31, 1997	JUNE 30, 1997	SEPTEMBER 30, 1997	DECEMBER 31, 1997
Net operating revenues..	\$50,237	\$64,583	\$73,333	\$84,794	\$89,030	\$104,752	\$113,668	\$130,755
Operating income.....	9,551	11,556	13,126	14,596	16,041	18,709	20,997	24,111
Income before extraordinary item ....	4,276	5,726	6,536	7,187	7,825	8,866	9,870	10,416
Net income (loss).....	4,276	5,726	(1,164)	7,187	7,825	8,866	9,870	10,416
Earning (loss) per common share:								
Income before extraordinary item per share.....	0.12	0.13	0.15	0.16	0.18	0.20	0.22	0.23
Extraordinary loss.....	0.00	0.00	(0.17)	0.00	0.00	0.00	0.00	0.00
Net income (loss) per share .....	0.12	0.13	(0.02)	0.16	0.18	0.20	0.22	0.23
Earnings (loss) per common share-- assuming dilution:.....								
Income before extraordinary item per share.....	0.11	0.13	0.15	0.16	0.17	0.20	0.22	0.23
Extraordinary loss.....	0.00	0.00	(0.17)	0.00	0.00	0.00	0.00	0.00
Net income (loss) per share.....	0.11	0.13	(0.02)	0.16	0.17	0.20	0.22	0.23

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

## 17. SUBSEQUENT EVENTS

On February 27, 1998 the Company acquired Renal Treatment Centers, Inc. ("RTC"), with headquarters in Berwyn, Pennsylvania ("Merger"). In connection with the Merger, the Company issued 34,565,729 shares of its common stock in exchange for all of the outstanding shares of RTC common stock. RTC shareholders received 1.335 shares of the Company's common stock for each share of RTC common stock that they owned. The Company also issued 2,156,424 options in substitution for previously outstanding RTC stock options, including 1,662,354 of the vested options that were exercised on the merger date or shortly thereafter. In addition, the Company guaranteed \$125,000,000 of RTC's 5 5/8% subordinated convertible notes. As a result of this transaction, the Board and the Company's stockholders authorized an additional 140,000,000 shares of common stock. The Merger will be accounted for as a pooling of interests and as such, the consolidated financial statements will be restated to include RTC for all periods presented.

The following unaudited pro forma combined condensed balance sheet presents the combined financial position of the Company and RTC as of December 31, 1997, and the following unaudited pro forma combined condensed statements of operations present the results of operations for the year ended May 31, 1995, the seven months ended December 31, 1995 and the years ended December 31, 1996 and 1997, in each case as previously announced by the Company and by RTC, respectively. The Company is reviewing the financial statements of RTC and has determined that the accounts receivable and certain other accounts recorded by RTC as of December 31, 1997 were overstated by an aggregate amount estimated to be between \$25 million and \$30 million. The Company has determined that at least some, and perhaps all, of such noncash charges will be recorded in 1997. This will require a revision of RTC's previously announced results of operations for 1997. Whether any portion of such noncash charges will be recorded in prior years has not yet been determined. The following unaudited pro forma combined condensed financial statements should be read in light of the uncertainty resulting from such review and preliminary determination. In addition, as with any pro forma financial statements, these unaudited pro forma combined condensed financial statements may not be indicative of the results to be expected in the future and do not reflect any changes in the operations of either the Company or RTC which may result from the combination of their operations or the significant one-time merger related costs which will be recorded in early 1998.

The following unaudited pro forma combined condensed financial statements combine the Company's balance sheet as of December 31, 1997 and the results of operations for the twelve months ended December 31, 1997 and 1996, the seven month period ended December 31, 1995 and the twelve months ended May 31, 1995 with RTC's balance sheet as of December 31, 1997 and the results of operations for the twelve months ended December 31, 1997 and 1996, the six months ended December 31, 1995 and the twelve months ended December 31, 1994, respectively.

PRO FORMA COMBINED CONDENSED BALANCE SHEET (UNAUDITED)  
DECEMBER 31, 1997

	TRCH	RTC	MERGER ADJUSTMENTS	PRO FORMA COMBINED
Cash and cash equivalents.....	\$ 5,400,000	\$ 1,565,000		\$ 6,965,000
Accounts receivable, net.....	152,481,000	124,564,000		277,045,000
Other current assets....	28,169,000	13,929,000		42,098,000
	-----	-----	-----	-----
Total current assets..	186,050,000	140,058,000		326,108,000
Property and equipment, net.....	100,061,000	72,604,000		172,665,000
Intangible assets, net..	389,737,000	382,744,000		772,481,000
Other assets.....	19,492,000	12,046,000	\$(2,600,000)(2)	28,938,000
	-----	-----	-----	-----
Total assets.....	\$695,340,000	\$607,452,000	\$(2,600,000)	\$1,300,192,000
	=====	=====	=====	=====
Current liabilities....	\$ 39,776,000	\$ 65,126,000		\$ 104,902,000
Long term debt.....	356,563,000	367,358,000		723,921,000
Other long-term liabilities.....	6,250,000		\$(2,600,000)(2)	3,650,000
Minority interests.....	19,079,000			19,079,000
Common stock.....	45,000	251,000	(218,000)(1)	78,000
Addition paid-in capital.....	261,810,000	96,852,000	(170,000)(1)	358,492,000
Notes receivable from stockholders.....	(3,030,000)			(3,030,000)
Retained earnings.....	14,847,000	78,253,000		93,100,000
Treasury stock.....		(388,000)	388,000 (1)	
	-----	-----	-----	-----
Total stockholders' equity.....	273,672,000	174,968,000		448,640,000
	-----	-----	-----	-----
Total liabilities and stockholders' equity.....	\$695,340,000	\$607,452,000	\$(2,600,000)	\$1,300,192,000
	=====	=====	=====	=====

(1) The unaudited pro forma combined condensed balance sheet gives effect to the proposed merger of TRCH and RTC by combining the respective balance sheets of the two companies as of December 31, 1997 on a pooling of interests basis. As shown above, the capital accounts have been adjusted as if 33,450,808 shares of common stock of TRCH (survivor) were issued in exchange for all of the outstanding shares of RTC. The difference between par value of RTC shares received in exchange and the par value of TRCH's shares issued has been charged to additional paid capital.

(2) For purposes of the unaudited pro forma combined condensed balance sheet, RTC's long term deferred tax asset from domestic operations is offset against the Company's long term deferred tax liability.



## TOTAL RENAL CARE HOLDINGS, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS--(CONTINUED)

## PRO FORMA COMBINED CONDENSED STATEMENT OF OPERATIONS (UNAUDITED)

	YEAR ENDED MAY 31, 1995	SEVEN MONTHS ENDED DEC. 31, 1995	YEARS ENDED DECEMBER 31, ----- 1996	1997
Net operating revenues				
TRCH.....	\$ 98,968,000	\$ 89,711,000	\$272,947,000	\$438,205,000
RTC.....	115,457,000	86,752,000	235,397,000	332,939,000
	-----	-----	-----	-----
	\$214,425,000	\$176,463,000	\$508,344,000	\$771,144,000
	=====	=====	=====	=====
Net income before extraordinary item				
TRCH.....	\$ 4,852,000	\$ 6,467,000	\$ 23,725,000	\$ 36,977,000
RTC.....	10,051,000	8,254,000	19,290,000	29,251,000
	-----	-----	-----	-----
	\$14,903,000	\$ 14,721,000	\$ 43,015,000	\$ 66,228,000
	=====	=====	=====	=====
Net income after extraordinary item				
TRCH.....	\$ 4,852,000	\$ 3,912,000	\$ 16,025,000	\$ 36,977,000
RTC.....	10,051,000	8,254,000	19,290,000	29,251,000
	-----	-----	-----	-----
	\$14,903,000	\$ 12,166,000	\$ 35,315,000	\$ 66,228,000
	=====	=====	=====	=====
Earnings per common share				
Income before extraordinary item.....	\$ 0.33	\$ 0.26	\$ 0.58	\$ 0.85
	=====	=====	=====	=====
Net Income.....	\$ 0.33	\$ 0.22	\$ 0.48	\$ 0.85
	=====	=====	=====	=====
Weighted average number of common shares outstanding.....	45,539,000	56,465,000	74,042,000	77,524,000
	=====	=====	=====	=====
Earnings per common share-- assuming dilution				
Income before extraordinary item.....	\$ 0.31	\$ 0.25	\$ 0.56	\$ 0.83
	=====	=====	=====	=====
Net income.....	\$ 0.31	\$ 0.20	\$ 0.46	\$ 0.83
	=====	=====	=====	=====
Weighted average number of common shares and equivalents outstanding--assuming dilution.....	48,087,000	60,049,000	77,225,000	79,975,000
	=====	=====	=====	=====

# SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized in the City of Torrance, State of California, on the 30th day of March, 1998.

TOTAL RENAL CARE HOLDINGS, INC.

/s/ Victor M.G. Chaltiel  
By: \_\_\_\_\_  
Victor M.G. Chaltiel  
Chairman of the Board,  
Chief Executive Officer and  
President

# POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Victor M.G. Chaltiel, Barry C. Cosgrove and John E. King, and each of them his or her true and lawful attorneys-in-fact and agents with full power of substitution and resubstitution, for him and in his name or for her and in her name, place and stead, in any and all capacities, to sign any and all amendments to this Report on Form 10-K, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or their or his or her substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report on Form 10-K has been signed by the following persons on behalf of the Registrant in the capacities and on the dates indicated.

SIGNATURE	TITLE	DATE
/s/ Victor M.G. Chaltiel	Chairman of the Board, Chief Executive Officer, President and Director (Principal Executive Officer)	March 30, 1998
Victor M.G. Chaltiel		
/s/ John E. King	Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	March 30, 1998
John E. King		
/s/ Maris Andersons	Director	March 30, 1998
Maris Andersons		
/s/ Peter T. Grauer	Director	March 30, 1998
Peter T. Grauer		
/s/ Regina E. Herzlinger	Director	March 30, 1998
Regina E. Herzlinger		
/s/ Shaul G. Massry	Director	March 30, 1998
Shaul G. Massry		

REPORT OF INDEPENDENT ACCOUNTANTS ON  
FINANCIAL STATEMENT SCHEDULE

To the Board of Directors  
of Total Renal Care Holdings, Inc.

Our audit of the consolidated financial statements referred to in our report dated February 16, 1998, except as to Note 17 which is as of March 30, 1998, appearing on page F-1 of this Annual Report on Form 10-K also included audits of the information included in the Financial Statement Schedule listed in Item 14(a)(2) of this Form 10-K for the year ended May 31, 1995, the seven months ended December 31, 1995 and the years ended December 31, 1996 and 1997. In our opinion, the Financial Statement Schedule presents fairly, in all material respects, the information for the year ended May 31, 1995, the seven months ended December 31, 1995 and the years ended December 31, 1996 and 1997 set forth therein when read in conjunction with the related consolidated financial statements.

PRICE WATERHOUSE LLP  
Seattle, Washington  
February 16, 1998

## TOTAL RENAL CARE HOLDINGS, INC.

## SCHEDULE II--VALUATION AND QUALIFYING ACCOUNTS

DESCRIPTION	BALANCE AT BEGINNING OF YEAR	ADDITIONS		DEDUCTIONS	
		AMOUNTS CHARGED TO INCOME	BALANCE OF COMPANIES ACQUIRED	AMOUNTS WRITTEN OFF	BALANCE AT END OF YEAR
Allowance for doubtful accounts:					
Year ended May 31, 1995.....	\$1,927,000	\$2,371,000	\$1,203,000	\$1,067,000	\$ 4,434,000
Seven months ended December 31, 1995.....	4,434,000	1,811,000	541,000	1,118,000	5,668,000
Year ended December 31, 1996.....	5,668,000	5,496,000	1,896,000	5,149,000	7,911,000
Year ended December 31, 1997.....	7,911,000	8,896,000	101,000	5,016,000	11,892,000

## EXHIBIT INDEX

(3)(a) Exhibits:

EXHIBIT NUMBER	DESCRIPTION	PAGE NUMBER
3.1	Amended and Restated Certificate of Incorporation of the Company, dated December 4, 1995.@@	
3.2	Certificate of Amendment of Certificate of Incorporation of the Company, dated February 26, 1998.X	
3.3	Bylaws of the Company, dated October 6, 1995.+	
4.1	Shareholders Agreement, dated August 11, 1994 between DLJMB, DLJIP, DLJOP, DLJMBF, NME Properties, Continental Bank, as voting trustee, and the Company.##	
4.2	Agreement and Amendment, dated as of June 30, 1995, between DLJMBP, DLJIP, DLJOP, DLJMBF, DLJESC, Tenet, the Company, Victor M.G. Chaltiel, the Putnam Purchasers, the Crescent Purchasers and the Harvard Purchasers, relating to the Shareholders Agreement dated as of August 11, 1994 between DLJMB, DLJIP, DLJOP, DLJMBF, NME Properties, Continental Bank, as voting trustee, and the Company.##	
10.1	Credit Agreement by and among the Company, the Lenders party thereto, BNY Capital Markets, Inc. and Donaldson Lufkin & Jenrette Securities Corporation as Arrangers, DLJ Capital Funding, Inc. as Documentation Agent and The Bank of New York as Administrative Agent, dated as of October 11, 1996 (the "TRCH Credit Facility").@	
10.2	Guaranty by Total Renal Care, Inc. to The Bank of New York, as Administrative Agent, pursuant to the TRCH Credit Facility.@	
10.3	Subscription Agreement dated May 26, 1994 between DLJMB, DLJIP, DLJOP, DLJMBF, NME Properties, Tenet and the Company.#	
10.4	Services Agreement dated August 11, 1994 between the Company and Tenet.##	
10.5	Noncompetition Agreement dated August 11, 1994 between the Company and Tenet.##	
10.6	Employment Agreement dated as of August 11, 1994 by and between the Company and Victor M.G. Chaltiel (with forms of Promissory Note and Pledge and Stock Subscription Agreement attached as exhibits thereto) (the "Chaltiel Employment Agreement").##*	
10.7	Amendment to Chaltiel Employment Agreement, dated as of August 11, 1994.##*	
10.8	Employment Agreement dated as of September 1, 1994 by and between the Company and Barry C. Cosgrove.##*	
10.9	Employment Agreement dated as of August 11, 1994 by and between the Company and Leonard W. Frie (the "Frie Employment Agreement").##*	
10.10	Amendment to Frie Employment Agreement, dated as of October 11, 1994.##*	
10.11	Employment Agreement dated as of September 1, 1994 by and between the Company and John E. King.##*	
10.12	First Amended and Restated 1994 Equity Compensation Plan (the "1994 Plan") of the Company (with form of Promissory Note and Pledge attached as an exhibit thereto), dated August 5, 1994.##*	
10.13	Form of Stock Subscription Agreement relating to the 1994 Plan.##*	
10.14	Form of Purchased Shares Award Agreement relating to the 1994 Plan.##*	
10.15	Form of Nonqualified Stock Option relating to the 1994 Plan.##*	
10.16	1995 Equity Compensation Plan.+*	

EXHIBIT NUMBER	DESCRIPTION	PAGE NUMBER
10.17	Employee Stock Purchase Plan.+*	
10.18	Option Exercise and Bonus Agreement dated as of September 18, 1995 between the Company and Victor M.G. Chaltiel.+*	
10.19	1997 Equity Compensation Plan.**	
10.20	Revolving Credit Agreement, dated as of October 24, 1997, by and among the Company, the lenders party thereto, DLJ Capital Funding, Inc., as Syndication Agent, First Union National Bank, as Documentation Agent, and The Bank of New York, as Administrative Agent (the "Revolving Credit Agreement").@@@	
10.21	Amendment No. 1 and Consent No. 1, dated as of December 1, 1997, to the Revolving Credit Agreement.@@@	
10.22	Term Loan Agreement, dated as of October 24, 1997, by and among the Company, the lenders party thereto, DLJ Capital Funding, Inc., as Syndication Agent, First Union National Bank, as Documentation Agent, and The Bank of New York, as Administrative Agent (the "Term Loan Agreement").@@@	
10.23	First Amendment, dated December 1, 1997, to the Term Loan Agreement.@@@	
10.24	Subsidiary Guaranty (the "Subsidiary Guaranty") dated as of October 24, 1997 by Total Renal Care, Inc., TRC West, Inc. and Total Renal Care Acquisition Corp. in favor of and for the benefit of The Bank of New York, as Collateral Agent, the lenders to the Revolving Credit Agreement, the lenders to the Term Loan Agreement, the Term Agent (as defined therein), the Acknowledging Interest Rate Exchangers (as defined therein) and the Acknowledging Currency Exchangers (as defined therein).@@@	
10.25	Borrower Pledge Agreement dated as of October 24, 1997 and entered into by and between the Company, and The Bank of New York, as Collateral Agent, the lenders to the Revolving Credit Agreement, the lenders to the Term Loan Agreement, the Term Agent (as defined therein), the Acknowledging Interest Rate Exchangers (as defined therein) and the Acknowledging Currency Exchangers (as defined therein).@@@	
10.26	Form of Subsidiary Pledge Agreement dated as of October 24, 1997 by Total Renal Care, Inc., TRC West, Inc. and Total Renal Care Acquisition Corp., and The Bank of New York, as Collateral Agent, the lenders to the Revolving Credit Agreement, the lenders to the Term Loan Agreement, the Term Agent (as defined therein), the Acknowledging Interest Rate Exchangers (as defined therein) and the Acknowledging Currency Exchangers (as defined therein).@@@	
10.27	Agreement and Plan of Merger dated as of November 18, 1997 by and among TRCH, Nevada Acquisition Corp., a Delaware corporation and wholly-owned subsidiary of TRCH, and RTC.###	
10.28	Second Amendment, dated January 13, 1998, to the Term Loan Agreement.X	
10.29	Amendment No. 2 and Consent No. 2 to the Revolving Credit Agreement and First Amendment to the Subsidiary Guaranty dated February 17, 1998.X	
10.30	Third Amendment to the Term Loan Agreement and First Amendment to the Subsidiary Guaranty dated February 17, 1998.X	
10.31	Special Purpose Option Plan.++	
10.32	Indenture, dated June 12, 1996, by RTC to PNC Bank including form of RTC Note (the "Indenture").***	
10.33	First Supplemental Indenture, dated as of February 27, 1998, among RTC, TRCH and PNC Bank under the Indenture.X	
10.34	Second Supplemental Indenture, dated as of March 31, 1998, among RTC, TRCH and PNC Bank under the Indenture.X	

10.35 Guaranty, entered into as of March 31, 1998, by TRCH in favor of and for  
the benefit of PNC Bank.X  
21 List of Subsidiaries of the Company.X  
23.1 Consent of Price Waterhouse LLP.X  
24 Powers of Attorney with respect to the Company (included on Page  
II-1 hereof).X  
27 Financial Data Schedule.X

- -----  
X Included in this filing.  
@ Filed on October 18, 1996 as an exhibit to the Company's Current Report on  
Form 8-K.  
@@ Filed on March 18, 1996 as an exhibit to the Company's Transitional Report  
on Form 10-K for the transition period from June 1, 1995 to December 31,  
1995.  
@@@ Filed on December 19, 1997 as an exhibit to the Company's Current Report  
on Form 8-K.  
+ Filed on October 24, 1995 as an exhibit to Amendment No. 2 to the Company's  
Registration Statement on Form S-1 (Registration Statement No. 33-97618).  
++ Filed on February 25, 1998 as an exhibit to the Company's Registration  
Statement on Form S-8 (Registration Statement No. 333-46887).  
# Filed on June 6, 1994 as an exhibit to the Company's Registration Statement  
on Form S-1 (Registration Statement No. 33-79770).  
## Filed on August 29, 1995 as an exhibit to the Company's Form 10-K for the  
year ended May 31, 1995.  
### Filed on December 19, 1997 as Annex A to the Company's Registration  
Statement on Form S-4 (Registration No. 333-42653).  
\* Management contract or executive compensation plan or arrangement.  
\*\* Filed on August 29, 1997 as an exhibit to the Company's Registration  
Statement on Form S-8 (Registration Statement No. 333-34695).  
\*\*\* Filed as an exhibit to RTC's Form 10-Q for the quarter ended June 30,  
1996.

CERTIFICATE OF AMENDMENT  
OF  
CERTIFICATE OF INCORPORATION  
OF  
TOTAL RENAL CARE HOLDINGS, INC.

Total Renal Care Holdings, Inc. (the "Corporation"), a corporation organized and existing under and by virtue of the General Corporation Law of the State of Delaware, does hereby certify:

FIRST: That the Corporation was originally incorporated under the name Medical Ambulatory Care Delaware, Inc., and the date of the filing of the Corporation's original Certificate of Incorporation with the Delaware Secretary of State was April 4, 1994.

SECOND: That the Board of Directors of the Corporation adopted a resolution proposing and declaring advisable the following amendment to the Corporation's Certificate of Incorporation:

"NOW, THEREFORE, BE IT RESOLVED, that the first paragraph of Article Fourth of the Company's Certificate of Incorporation be amended to read in its entirety as follows (the "Amendment"):

"A. SHARES AUTHORIZED. The total number of shares of all classes of stock which the Corporation shall have the authority to issue is Two Hundred Million (200,000,000) shares consisting of One Hundred Ninety-Five Million (195,000,000) shares of Common Stock, par value \$0.001 per share (the "Common Stock"), and Five Million (5,000,000) shares of Preferred Stock, par value \$0.001 per share (the "Preferred Stock")."

THIRD: That the foregoing amendment was duly adopted by all of the duly elected directors of the Corporation in accordance with the applicable provisions of Section 242 of the General Corporation Law of the State of Delaware.

FOURTH: The foregoing amendment was duly adopted by a majority of the outstanding shares of stock of the Corporation in accordance with the applicable provisions of Section 242 of the General Corporation Law of the State of Delaware and the Corporation's Certificate of Incorporation.



IN WITNESS WHEREOF, the Corporation has caused this Certificate to be signed  
by Barry C. Cosgrove, its Vice President, General Counsel and Secretary, this  
26th day of February, 1998.

TOTAL RENAL CARE HOLDINGS, INC.,  
a Delaware corporation

By:

-----

Barry C. Cosgrove,  
Vice President, General Counsel  
and Secretary

56101.1

## TOTAL RENAL CARE HOLDINGS, INC.

SECOND AMENDMENT  
TO TERM LOAN AGREEMENT

This SECOND AMENDMENT TO TERM LOAN AGREEMENT (this "AMENDMENT") is dated as of January 13, 1998, and entered into by and among TOTAL RENAL CARE HOLDINGS, INC., a Delaware corporation (the "Borrower"), the financial institutions listed on the signature pages hereof and their respective successors and assigns (the "Lenders", each a "Lender"), DLJ CAPITAL FUNDING, INC., as Syndication Agent (the "Syndication Agent"), THE BANK OF NEW YORK, as administrative agent for the Lenders (in such capacity, the "Administrative Agent"), and, for purposes of Section 4 hereof, the Credit Support Parties (as defined in Section 4 hereof) listed on the signature pages hereof, and is made with reference to that certain Term Loan Agreement dated as of October 24, 1997, as amended by that certain First Amendment to Term Loan Agreement dated as of December 1, 1997 (said agreement, as so amended, being the "TERM LOAN AGREEMENT"), by and among Borrower, Lenders, Syndication Agent and Administrative Agent. Capitalized terms used herein without definition shall have the same meanings herein as set forth in the Term Loan Agreement.

## RECITALS

WHEREAS, Borrower and Lenders desire to amend the Term Loan Agreement in order to (i) revise the definition of "Subordinated Indebtedness" contained therein, (ii) revise certain negative covenants regarding amendments to Subordinated Indebtedness and (iii) make certain other changes as set forth herein.

NOW, THEREFORE, in consideration of the premises and the agreements, provisions and covenants herein contained, the parties hereto agree as follows:

## SECTION 1. AMENDMENTS TO THE TERM LOAN AGREEMENT

## 1.1 Amendments to Section 1: Provisions Relating to Defined Terms

A. Subsection 1.1 of the Term Loan Agreement is hereby amended by the definition of "Subordinated Indebtedness" therefrom in its entirety and substituting the following therefor:

"Subordinated Indebtedness": any unsecured Indebtedness of the Borrower subordinated in right of payment to the payment in full of the Obligations of the Borrower and other senior obligations of the Borrower; provided that (i) the negative covenants in such Indebtedness are less restrictive than the negative covenants in this Agreement as in effect at the time such Indebtedness is incurred, (ii) the affirmative covenants in such Indebtedness are no more restrictive than the affirmative covenants in this Agreement as in effect at the time such Indebtedness is incurred, (iii) the events of default in such Indebtedness relating to insolvency and nonpayment of amounts owed thereunder are no more restrictive than the corresponding defaults in this Agreement as in effect at the time such Indebtedness is incurred, and the other events of default in such Indebtedness are less restrictive than the corresponding defaults in this Agreement as in effect at the time such Indebtedness is incurred, (iv) such Indebtedness does not cross-default to other Indebtedness (but may cross-accelerate to other Indebtedness of Borrower or any Subsidiary Guarantor that has guaranteed such Indebtedness), (v) the subordination provisions in such Indebtedness are on market terms for subordinated debt instruments prevailing at or around the time such Indebtedness is incurred and (vi) such Indebtedness provides for no scheduled payment or mandatory prepayments of principal before March 30, 2008, other than (x) redemptions made at the option of the holders of such Indebtedness upon a change in control of the Borrower in circumstances where the holders of the Term Loans would have rights to prepayment under Section 2.4(c), provided that any such redemptions are made not fewer than 30 days after such change in control and (y) mandatory prepayments required as a result of asset dispositions if such

Indebtedness allows the Borrower to satisfy such mandatory prepayment requirement by prepayment of senior obligations of the Borrower or reinvestment of the asset disposition proceeds within a specified period of time.

## 1.2 Amendments to Section 8: Negative Covenants

A. Section 8.1(b) of the Term Loan Agreement is hereby amended by (i) deleting the "and" at the end of clause (xii) thereof, (ii) relabeling clause (xiii) thereof as clause (xiv) and (iii) adding a new clause (xiii) thereto as follows:

"(xiii) Guaranties by any Guarantor of Borrower's obligations under any Subordinated Indebtedness permitted hereunder, provided that (a) all Obligations of Borrower are guarantied by such Guarantor under the Subsidiary Guaranty, (b) each such Guaranty is subordinated to at least the same extent as the Subordinated Indebtedness guarantied thereby is subordinated to the Obligations of Borrower, (c) each such Guaranty contains a limitation as to maximum amount guarantied thereby similar to that set forth in subsection 2.2(a) of the Subsidiary Guaranty, provided that in no event shall the liability of the Guarantor under such Guaranty exceed the maximum amount permissible under applicable fraudulent conveyance or similar law, and (d) each such Guaranty is otherwise on market terms for guaranties of subordinated debt instruments prevailing at or around the time such Guaranties are entered into; and".

B. Section 8.5 of the Term Loan Agreement is hereby amended by (i) deleting the "and" at the end of clause (k) thereof, (ii) relabeling clause (l) thereof as clause (m) and (iii) adding a new clause (l) thereto as follows:

"(l) Contingent Obligations to the extent permitted by Section 8.1(b); and".

C. Section 8.15 of the Term Loan Agreement is hereby amended by adding a new subsection (d) thereto as follows:

"(d) The Borrower will not, and will not permit any of its Subsidiaries to, amend or otherwise change the terms of any Subordinated Indebtedness, or make any payment consistent with an amendment thereof or change thereto, if the effect of such amendment or change is to change (to any date before March 30, 2008) any dates upon which payments of principal are due thereon, change the redemption, prepayment or defeasance provisions thereof (unless the redemption or prepayment provisions as so changed would be permitted under clause (vi) of the definition of "Subordinated Indebtedness"), change the subordination provisions thereof (or of any guaranty thereof), or grant any Lien to secure payment thereof, or if the effect of such amendment or change, together with all other amendments or changes made, is to increase materially the obligations of the obligor thereunder or to confer any additional rights on the holders of such Subordinated Indebtedness (or a trustee or other representative on their behalf) which would be adverse to the Borrower or Lenders."

## SECTION 2. CONDITIONS TO EFFECTIVENESS

Section 1 of this Amendment shall become effective only upon the satisfaction of all of the following conditions precedent (the date of satisfaction of such conditions being referred to herein as the "SECOND AMENDMENT EFFECTIVE DATE"):

A. All fees and expenses incurred by Syndication Agent and its counsel, O'Melveny & Myers LLP, in connection with the preparation, negotiation and closing of this Amendment shall have been paid by Borrower.

B. All fees and expenses incurred by Administrative Agent and its counsel, Emmet, Marvin & Martin, LLP, in connection with the preparation, negotiation and closing of this Amendment shall have been paid by Borrower.

### SECTION 3. BORROWER'S REPRESENTATIONS AND WARRANTIES

In order to induce Lenders to enter into this Amendment and to amend the Term Loan Agreement in the manner provided herein, Borrower represents and warrants to each Lender that the following statements are true, correct and complete:

A. CORPORATE POWER AND AUTHORITY. Each Credit Party has all requisite corporate power and authority to enter into this Amendment and to carry out the transactions contemplated by, and perform its obligations under, the Term Loan Agreement as amended by this Amendment (the "AMENDED AGREEMENT").

B. AUTHORIZATION OF AGREEMENTS. The execution and delivery of this Amendment have been duly authorized by all necessary corporate action on the part of each Credit Party. The performance of the Amended Agreement has been duly authorized by all necessary corporate action on the part of each Credit Party.

C. NO CONFLICT. The execution and delivery by each Credit Party of this Amendment, and the performance by each Credit Party of the Amended Agreement do not and will not (i) violate any provision of any law or any governmental rule or regulation applicable to Borrower or any of its Subsidiaries, the Certificate or Articles of Incorporation or Bylaws of Borrower or any of its Subsidiaries or any order, judgment or decree of any court or other agency of government binding on Borrower or any of its Subsidiaries, (ii) conflict with, result in a breach of or constitute (with due notice or lapse of time or both) a default under any contractual obligation of Borrower or any of its Subsidiaries, (iii) result in or require the creation or imposition of any Lien upon any of the properties or assets of Borrower or any of its Subsidiaries (other than Liens created under any of the Loan Documents in favor of Administrative Agent on behalf of Lenders), or (iv) require any approval of stockholders or any approval or consent of any Person under any contractual obligation of Borrower or any of its Subsidiaries.

D. GOVERNMENTAL CONSENTS. The execution and delivery by each Credit Party of this Amendment, and the performance by each Credit Party of the Amended Agreement do not and will not require any registration with, consent or approval of, or notice to, or other action to, with or by, any federal, state or other governmental authority or regulatory body.

E. BINDING OBLIGATION. This Amendment and the Amended Agreement have been duly executed and delivered by each Credit Party and are the legally valid and binding obligations of each Credit Party, enforceable against each Credit Party in accordance with their respective terms, except as may be limited by bankruptcy, insolvency, reorganization, moratorium or similar laws relating to or limiting creditors' rights generally or by equitable principles relating to enforceability.

F. INCORPORATION OF REPRESENTATIONS AND WARRANTIES FROM TERM LOAN AGREEMENT. The representations and warranties contained in Section 4 of the Term Loan Agreement are and will be true, correct and complete in all material respects on and as of the Second Amendment Effective Date to the same extent as though made on and as of that date, except to the extent such representations and warranties specifically relate to an earlier date, in which case they were true, correct and complete in all material respects on and as of such earlier date.

G. ABSENCE OF DEFAULT. No event has occurred and is continuing or will result from the consummation of the transactions contemplated by this Amendment that would constitute an Event of Default.

### SECTION 4. ACKNOWLEDGEMENT AND CONSENT

Borrower is a party to the Borrower Pledge Agreement pursuant to which Borrower has pledged certain Collateral to Administrative Agent to secure the Obligations. TRC is a party to the Subsidiary Guaranty and the Subsidiary Pledge Agreement pursuant to which TRC has (i) guaranteed the Obligations and (ii) pledged certain Collateral to Administrative Agent to secure the Obligations and to secure the obligations of TRC under the Subsidiary Guaranty. TRC West, Inc. is a party to the Subsidiary Guaranty pursuant to which TRC West, Inc. has guaranteed the Obligations. Total Renal Care Acquisition Corp. is a party to the Subsidiary Guaranty pursuant

to which Total Renal Care Acquisition Corp. has guaranteed the Obligations. Borrower, TRC, TRC West, Inc. and Total Renal Care Acquisition Corp. are collectively referred to herein as the "CREDIT SUPPORT PARTIES", and the Borrower Pledge Agreement, the Subsidiary Pledge Agreement and the Subsidiary Guaranty are collectively referred to herein as the "CREDIT SUPPORT DOCUMENTS".

Each Credit Support Party hereby acknowledges that it has reviewed the terms and provisions of the Term Loan Agreement and this Amendment and consents to the amendment of the Term Loan Agreement effected pursuant to this Amendment. Each Credit Support Party hereby confirms that each Credit Support Document to which it is a party or otherwise bound and all Collateral encumbered thereby will continue to guaranty or secure, as the case may be, to the fullest extent possible the payment and performance of all "Guarantied Obligations" and "Secured Obligations," as the case may be (in each case as such terms are defined in the applicable Credit Support Document), including without limitation the payment and performance of all such "Guarantied Obligations" and "Secured Obligations," as the case may be, in respect of the Obligations of Borrower now or hereafter existing under or in respect of the Amended Agreement and the Notes defined therein.

Each Credit Support Party acknowledges and agrees that any of the Credit Support Documents to which it is a party or otherwise bound shall continue in full force and effect and that all of its obligations thereunder shall be valid and enforceable and shall not be impaired or limited by the execution or effectiveness of this Amendment. Each Credit Support Party represents and warrants that all representations and warranties contained in the Amended Agreement and the Credit Support Documents to which it is a party or otherwise bound are true, correct and complete in all material respects on and as of the Second Amendment Effective Date to the same extent as though made on and as of that date, except to the extent such representations and warranties specifically relate to an earlier date, in which case they were true, correct and complete in all material respects on and as of such earlier date.

Each Credit Support Party acknowledges and agrees that (i) notwithstanding the conditions to effectiveness set forth in this Amendment, such Credit Support Party is not required by the terms of the Term Loan Agreement or any other Loan Document to consent to the amendments to the Term Loan Agreement effected pursuant to this Amendment and (ii) nothing in the Term Loan Agreement, this Amendment or any other Loan Document shall be deemed to require the consent of such Credit Support Party to any future amendments to the Term Loan Agreement.

#### SECTION 5. MISCELLANEOUS

##### A. REFERENCE TO AND EFFECT ON THE TERM LOAN AGREEMENT AND THE OTHER LOAN DOCUMENTS.

(i) On and after the Second Amendment Effective Date, each reference in the Term Loan Agreement to "this Agreement", "hereunder", "hereof", "herein" or words of like import referring to the Term Loan Agreement, and each reference in the other Loan Documents to the "Term Loan Agreement", "thereunder", "thereof" or words of like import referring to the Term Loan Agreement shall mean and be a reference to the Amended Agreement.

(ii) Except as specifically amended by this Amendment, the Term Loan Agreement and the other Loan Documents shall remain in full force and effect and are hereby ratified and confirmed.

(iii) The execution, delivery and performance of this Amendment shall not, except as expressly provided herein, constitute a waiver of any provision of, or operate as a waiver of any right, power or remedy of Administrative Agent or any Lender under, the Term Loan Agreement or any of the other Loan Documents.

B. FEES AND EXPENSES. Borrower acknowledges that all costs, fees and expenses as described in Section 11.5 of the Term Loan Agreement incurred by Administrative Agent, Syndication Agent, Co-Arrangers, Special Counsel, and Emmet, Marvin and Martin, LLP with respect to this Amendment and the documents and transactions contemplated hereby shall be for the account of Borrower.

C. HEADINGS. Section and subsection headings in this Amendment are included herein for convenience of reference only and shall not constitute a part of this Amendment for any other purpose or be given any substantive effect.

D. APPLICABLE LAW. THIS AMENDMENT AND THE RIGHTS AND OBLIGATIONS OF THE PARTIES HEREUNDER SHALL BE GOVERNED BY, AND SHALL BE CONSTRUED AND ENFORCED IN ACCORDANCE WITH, THE INTERNAL LAWS OF THE STATE OF NEW YORK (INCLUDING WITHOUT LIMITATION SECTION 5-1401 OF THE GENERAL OBLIGATIONS LAW OF THE STATE OF NEW YORK), WITHOUT REGARD TO CONFLICTS OF LAWS PRINCIPLES.

E. COUNTERPARTS; EFFECTIVENESS. This Amendment may be executed in any number of counterparts and by different parties hereto in separate counterparts, each of which when so executed and delivered shall be deemed an original, but all such counterparts together shall constitute but one and the same instrument; signature pages may be detached from multiple separate counterparts and attached to a single counterpart so that all signature pages are physically attached to the same document. This Amendment (other than the provisions of Section 1 hereof, the effectiveness of which is governed by Section 2 hereof) shall become effective upon the execution of a counterpart hereof by Borrower, Required Lenders, Administrative Agent, and each of the Credit Support Parties and receipt by Borrower and Administrative Agent of written or telephonic notification of such execution and authorization of delivery thereof.

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]

IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first written above.

BORROWER: TOTAL RENAL CARE HOLDINGS, INC.  
By: \_\_\_\_\_  
Title: V/P Finance & CFO

CREDIT SUPPORT PARTIES: TOTAL RENAL CARE, INC., (for  
purposes of  
Section 4 only) as a Credit Support  
Party

By: \_\_\_\_\_  
Title: V/P Finance & CFO

TRC WEST, INC., (for purposes of  
Section 4 only) as a Credit Support  
Party

By: \_\_\_\_\_  
Title: President

TOTAL RENAL CARE ACQUISITION CORP.,  
(for purposes of Section 4 only) as  
a Credit Support Party

By: \_\_\_\_\_  
Title: V/P Finance & CFO

AGENTS: THE BANK OF NEW YORK, Individually  
and as  
Administrative Agent

By: \_\_\_\_\_  
Title: Vice President

DLJ CAPITAL FUNDING, INC.,  
Individually and as Syndication  
Agent

By: \_\_\_\_\_  
Title: \_\_\_\_\_

LENDERS:

BDC FINANCE, LLC

By: \_\_\_\_\_  
Title: \_\_\_\_\_

CITIBANK, N.A.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

CONTINENTAL ASSURANCE COMPANY  
Separate Account (E)

By: TCW Asset Management Company, as  
Attorney-In-Fact, as Assignee

By: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Title: \_\_\_\_\_

DEBT STRATEGIES FUND, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_



DEEPROCK & COMPANY

By: Eaton Vance Management as  
Investment Advisor

By: \_\_\_\_\_  
Title: Vice President

FRANKLIN FLOATING RATE TRUST

By: \_\_\_\_\_  
Title: \_\_\_\_\_

KZH HOLDING CORPORATION III

By: \_\_\_\_\_  
Title: Authorized Agent

KZH--CRESCENT CORPORATION

By: \_\_\_\_\_  
Title: Authorized Agent

KZH--SOLEIL CORPORATION

By: \_\_\_\_\_  
Title: Authorized Agent

LEHMAN COMMERCIAL PAPER INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

MERRILL LYNCH SENIOR FLOATING RATE  
FUND, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

MORGAN STANLEY SENIOR FUNDING, INC.

By: \_\_\_\_\_  
Title: Vice President

OCTAGON CREDIT INVESTORS LOAN  
PORTFOLIO (a unit of The Chase  
Manhattan Bank)

By: \_\_\_\_\_  
Title: Managing Director

ORIX USA CORP.

By: \_\_\_\_\_  
Title: Executive Vice President

PARIBAS CAPITAL FUNDING LLC

By: \_\_\_\_\_  
Title: Director

PILGRIM AMERICA PRIME RATE TRUST

By: \_\_\_\_\_  
Title: \_\_\_\_\_

PIMCO HIGH YIELD FUND (Acct 705)

By: Pacific Investment Management  
Company, as its Investment  
Advisor acting through Investors  
Fiduciary Trust Company in the  
Nominee Name of IFTCO

By: \_\_\_\_\_  
Title: \_\_\_\_\_

SENIOR DEBT PORTFOLIO

By: Boston Management and Research,  
as Investment Advisor

By: \_\_\_\_\_  
Title: Vice President

SENIOR HIGH INCOME PORTFOLIO, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

T. ROWE PRICE HIGH YIELD FUND INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

VAN KAMPEN AMERICAN CAPITAL PRIME  
RATE INCOME TRUST

By: \_\_\_\_\_  
Title: Vice President

AMENDMENT NO. 2 AND CONSENT NO. 2  
TO REVOLVING CREDIT AGREEMENT AND  
AMENDMENT NO. 1 TO SUBSIDIARY GUARANTY

AMENDMENT NO. 2 and CONSENT NO. 2, dated as of February 17, 1998, to the Revolving Credit Agreement, as amended by Amendment No.1 and Consent No. 1, dated as of December 1, 1997 (the "Revolving Credit Agreement"), dated as of October 24, 1997, by and among TOTAL RENAL CARE HOLDINGS, INC., a Delaware corporation (the "Borrower"), the lenders party thereto (the "Lenders"), DLJ CAPITAL FUNDING, INC., as Syndication Agent (the "Syndication Agent"), FIRST UNION NATIONAL BANK, as Documentation Agent, and THE BANK OF NEW YORK, as administrative agent (in such capacity, the "Administrative Agent"), and AMENDMENT NO. 1, dated as of February 17, 1998, to the Subsidiary Guaranty, entered into as of October 24, 1997 (the "Subsidiary Guaranty"), by the GUARANTORS party thereto in favor of THE BANK OF NEW YORK, as collateral agent (in such capacity, the "Collateral Agent")(this "Amendment").

RECITALS

I. Capitalized terms used herein which are not otherwise defined herein shall have the respective meanings ascribed thereto in the Revolving Credit Agreement.

II. The Borrower has requested that the Administrative Agent and the Lenders agree to amend the Revolving Credit Agreement, among other things, to permit the Borrower to guaranty, on a subordinated basis, the obligations of RTC under the 5-5/8% Notes upon the terms and conditions contained herein, and the Administrative Agent and the Required Lenders are willing to so agree.

III. The Borrower has requested that the Collateral Agent and the Lenders agree to amend the Subsidiary Guaranty to designate the Subsidiary Guaranty as "Designated Senior Indebtedness" under the 5-5/8% Indenture upon the terms and conditions contained herein, and the Collateral Agent and the Required Lenders are willing to so agree.

Accordingly, in consideration of the Recitals and the covenants and conditions hereinafter set forth, and for other good and valuable consideration, the receipt and adequacy of which are hereby acknowledged, the parties hereto hereby agree as follows:

1. Section 1.1 of the Revolving Credit Agreement is amended by amending and restating in its entirety the definition of "Letter of Credit" as follows:

"Letter of Credit": as defined in Section 2.19, provided that each of the following shall constitute a Letter of Credit for the purposes of this Agreement: (i) each of the Existing Letters of Credit and (ii) effective upon the consummation of the Permitted Merger, the letter of credit no. S111397 in the amount of \$800,000, dated January 22, 1997, issued by First Union National Bank (formerly known as First Union National Bank of North Carolina) to Mutual Indemnity (Bermuda) Ltd. for the account of RTC, as such letter of credit may be renewed from time to time in accordance with its terms.

2. Section 1.1 of the Revolving Credit Agreement is amended by amending and restating in its entirety the definition of "Letter of Credit Issuer" as follows:

"Letter of Credit Issuer": BNY (or any successor thereto) and, solely for purposes of the Letter of Credit referred to in clause (ii) of the definition of "Letter of Credit", First Union National Bank (or any successor thereto).

3. Section 1.1 of the Revolving Credit Agreement is amended by adding the following definition in appropriate alphabetical order:

"5 5/8% Guaranty": The guaranty by the Borrower of RTC's obligations under the 5 5/8% Notes, provided that (i) such guaranty is subordinated to at least the same extent as the Indebtedness under the 5 5/8% Notes is subordinated to the Guaranteed Obligations (as such term is defined in the Subsidiary Guaranty) of RTC under the Subsidiary Guaranty, (ii) such guaranty is otherwise on market terms for guaranties of subordinated debt instruments prevailing at or around the time such guaranty is entered into and (iii) such guaranty is in form and substance satisfactory to the Administrative Agent and the Syndication Agent, as such guaranty may be amended, supplemented or otherwise modified from time to time in accordance with Section 8.9.

4. Section 4 of the Revolving Credit Agreement is amended by adding a new Section 4.22 thereto as follows:

#### 4.22 Subordinated Indebtedness

The subordination provisions of the 5 5/8% Indenture, the 5 5/8% Notes and the 5 5/8% Guaranty will be enforceable against the holders thereof, and the Loans and all other monetary obligations hereunder and all monetary obligations under the Subsidiary Guaranty will constitute "Senior Indebtedness" and "Designated Senior Indebtedness" (or any comparable terms) as defined in such provisions.

5. Section 8.1 of the Revolving Credit Agreement is amended by 1. deleting the word "and" immediately before clause (xvi) of such Section 8.1 and 2. inserting the following immediately prior to the period at the end of such Section 8.1:

, and (xvii) the 5 5/8% Guaranty.

6. Section 8.5 of the Revolving Credit Agreement is amended by 1. deleting the word "and" immediately before clause (l) to Section 8.5 and 2. inserting the following immediately prior to the period at the end of such Section 8.5:

; and (m) Contingent Obligations to the extent permitted by Section 8.1.

7. Section 8.9(d) of the Revolving Credit Agreement is hereby amended by 1. deleting the words "5 5/8% Indenture or the 5 5/8% Notes" and 2. substituting in their place the following:

5 5/8% Indenture, the 5 5/8% Notes or the 5 5/8% Guaranty.

8. Section 11 of the Revolving Credit Agreement is amended by adding a new Section 11.22 thereto as follows:

#### 11.22 Designation as Designated Senior Indebtedness

This Agreement, the Subsidiary Guaranty, and all Loans and all other monetary obligations hereunder and thereunder, are hereby expressly designated as "Designated Senior Indebtedness", as that term is defined in the 5 5/8% Indenture and in the 5 5/8% Guaranty.

9. The Subsidiary Guaranty is amended by adding a new Section 4.15 thereto as follows:

#### 4.15 Designation as Designated Senior Indebtedness; Incorporation of Defaults

This Guaranty, the Financing Documents, and all monetary obligations hereunder and thereunder, are hereby expressly designated as "Designated Senior Indebtedness", as that term is defined in the 5 5/8% Indenture. The occurrence of any Default or Event of Default constitutes a default under this Guaranty.

10. The Administrative Agent and the Lenders, to the extent their consent is required, hereby consent to the amendment of the Term Loan Facility substantially in the form of Exhibit A attached hereto (the "Third Term Loan Amendment").

11. Paragraphs 1-10 of this Amendment shall not be effective until such date as each of the following conditions shall have been satisfied:

(a). The Third Term Loan Amendment shall have become effective, and the Administrative Agent shall have received a certificate of an Authorized Signatory of the Borrower attaching a true, complete and correct copy of the fully executed Third Term Loan Amendment.

(b). The Borrower shall have paid the reasonable fees and disbursements of Special Counsel which shall have accrued up to the date hereof.

12. On the date hereof, each Credit Party hereby (a) reaffirms and admits the validity and enforceability of the Loan Documents (as amended by this Amendment) and all of its obligations thereunder, (b) agrees and admits that it has no defenses to or offsets against any such obligation, and (c) represents and warrants that no Default or Event of Default has occurred and is continuing, and that each of the representations and warranties made by it in the Loan Documents (as amended by this Amendment) to which it is a party is true and correct with the same effect as though such representation and warranty had been made on the date hereof.

13. In all other respects, the Loan Documents shall remain in full force and effect, and no amendment in respect of any term or condition of any Loan Document contained herein shall be deemed to be an amendment in respect of any other term or condition contained in any Loan Document.

14. This Amendment may be executed in any number of counterparts all of which, taken together, shall constitute one Amendment. In making proof of this Amendment, it shall only be necessary to produce the counterpart executed and delivered by the party to be charged.

15. THIS AMENDMENT IS BEING EXECUTED AND DELIVERED IN, AND IS INTENDED TO BE PERFORMED IN, THE STATE OF NEW YORK AND SHALL BE CONSTRUED AND ENFORCEABLE IN ACCORDANCE WITH, AND BE GOVERNED BY, THE INTERNAL LAWS OF THE STATE OF NEW YORK, WITHOUT REGARD TO PRINCIPLES OF CONFLICT OF LAWS.

AMENDMENT NO. 2 AND CONSENT NO. 2  
TO REVOLVING CREDIT AGREEMENT AND  
AMENDMENT NO. 1 TO SUBSIDIARY GUARANTY

AS EVIDENCE of the agreement by the parties hereto to the terms and conditions herein contained, each such party has caused this Amendment to be executed on its behalf.

TOTAL RENAL CARE HOLDINGS, INC.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

THE BANK OF NEW YORK,  
Individually, as a Letter of Credit  
Issuer, as the Swing Line Lender,  
as Administrative Agent and as  
Collateral Agent

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

DLJ CAPITAL FUNDING, INC.,  
Individually and as Syndication  
Agent

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

FIRST UNION NATIONAL BANK,  
Individually, as a Letter of Credit  
Issuer and as Documentation Agent

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

AMENDMENT NO. 2 AND CONSENT NO. 2  
TO REVOLVING CREDIT AGREEMENT AND  
AMENDMENT NO. 1 TO SUBSIDIARY GUARANTY

ABN AMRO BANK N.V.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

ALLIED IRISH BANKS, P.L.C., CAYMAN  
ISLANDS BRANCH

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

BANK LEUMI TRUST COMPANY OF NEW YORK

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

BANK OF MONTREAL

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_



AMENDMENT NO. 2 AND CONSENT NO. 2  
TO REVOLVING CREDIT AGREEMENT AND  
AMENDMENT NO. 1 TO SUBSIDIARY GUARANTY

THE BANK OF NOVA SCOTIA

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

BANQUE NATIONALE DE PARIS

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

BANQUE PARIBAS

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

CITY NATIONAL BANK

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

CORESTATES BANK N.A.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

AMENDMENT NO. 2 AND CONSENT NO. 2  
TO REVOLVING CREDIT AGREEMENT AND  
AMENDMENT NO. 1 TO SUBSIDIARY GUARANTY

CREDIT LYONNAIS NEW YORK BRANCH

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

DEUTSCHE BANK AG, NEW YORK AND/OR  
CAYMAN ISLANDS BRANCHES

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

DRESDNER BANK AG, NEW YORK BRANCH  
AND GRAND CAYMAN BRANCH

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

FLEET NATIONAL BANK

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

AMENDMENT NO. 2 AND CONSENT NO. 2  
TO REVOLVING CREDIT AGREEMENT AND  
AMENDMENT NO. 1 TO SUBSIDIARY GUARANTY

THE FUJI BANK, LIMITED

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

HIBERNIA NATIONAL BANK

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

THE INDUSTRIAL BANK OF JAPAN, LTD.,  
LOS ANGELES AGENCY

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

LONG TERM CREDIT BANK OF JAPAN, LTD.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

MELLON BANK, N.A.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

MICHIGAN NATIONAL BANK

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

AMENDMENT NO. 2 AND CONSENT NO. 2  
TO REVOLVING CREDIT AGREEMENT AND  
AMENDMENT NO. 1 TO SUBSIDIARY GUARANTY

THE MITSUBISHI TRUST AND BANKING  
CORPORATION

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

NATIONAL CITY BANK OF KENTUCKY

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

COOPERATIEVE CENTRALE RAIFFEISEN--  
BOERENLEENBANK B.A, "RABOBANK  
NEDERLAND", NEW YORK BRANCH

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

ROYAL BANK OF CANADA

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

THE ROYAL BANK OF SCOTLAND PLC

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

AMENDMENT NO. 2 AND CONSENT NO. 2  
TO REVOLVING CREDIT AGREEMENT AND  
AMENDMENT NO. 1 TO SUBSIDIARY GUARANTY

THE SAKURA BANK, LIMITED

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

THE SANWA BANK, LIMITED

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

SOCIETE GENERALE

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

THE SUMITOMO BANK, LIMITED, CHICAGO  
BRANCH

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

THE SUMITOMO TRUST & BANKING CO.,  
LTD., NEW YORK BRANCH

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

AMENDMENT NO. 2 AND CONSENT NO. 2  
TO REVOLVING CREDIT AGREEMENT AND  
AMENDMENT NO. 1 TO SUBSIDIARY GUARANTY

SUNTRUST BANK, NASHVILLE, N.A.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

THE TOYO TRUST & BANKING CO., LTD.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

UNION BANK OF CALIFORNIA, N.A.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

U.S. BANK NATIONAL ASSOCIATION

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

AMENDMENT NO. 2 AND CONSENT NO. 2  
TO REVOLVING CREDIT AGREEMENT AND  
AMENDMENT NO. 1 TO SUBSIDIARY GUARANTY

AGREED AND CONSENTED TO:

TOTAL RENAL CARE, INC.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

TRC WEST, INC.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

TOTAL RENAL CARE ACQUISITION CORP.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

TOTAL RENAL CARE HOLDINGS, INC.

THIRD AMENDMENT TO TERM LOAN AGREEMENT  
AND FIRST AMENDMENT TO SUBSIDIARY GUARANTY

This THIRD AMENDMENT TO TERM LOAN AGREEMENT AND FIRST AMENDMENT TO SUBSIDIARY GUARANTY (this "AMENDMENT") is dated as of February 17, 1998, and entered into by and among TOTAL RENAL CARE HOLDINGS, INC., a Delaware corporation (the "Borrower"), the financial institutions listed on the signature pages hereof and their respective successors and assigns (the "Lenders", each a "Lender"), DLJ CAPITAL FUNDING, INC., as Syndication Agent (the "Syndication Agent"), THE BANK OF NEW YORK, as collateral agent and as administrative agent for the Lenders (in such capacity, the "Administrative Agent"), and, for purposes of Sections 2 and 5 hereof, the Credit Support Parties (as defined in Section 5 hereof) listed on the signature pages hereof, and is made with reference to that certain Term Loan Agreement dated as of October 24, 1997, as amended by that certain First Amendment to Term Loan Agreement dated as of December 1, 1997 and that certain Second Amendment to Term Loan Agreement dated as of January 13, 1998 (as so amended, the "TERM LOAN AGREEMENT"), by and among Borrower, Lenders, Syndication Agent and Administrative Agent. Capitalized terms used herein without definition shall have the same meanings herein as set forth in the Term Loan Agreement.

RECITALS

WHEREAS, Borrower and Lenders desire to amend the Term Loan Agreement to permit Borrower to guaranty, on a subordinated basis, obligations of RTC under the RTC Convertible Subordinated Notes on and after the effectiveness of the RTC Merger Agreement;

WHEREAS, the Subsidiary Guarantors and the Collateral Agent desire to amend the Subsidiary Guaranty to provide that the obligations thereunder are expressly designated as "Designated Senior Indebtedness," as that term is defined in the RTC Convertible Subordinated Indenture; and

WHEREAS, subject to the terms and conditions of this Amendment, Lenders are willing to agree to such amendments.

NOW, THEREFORE, in consideration of the premises and the agreements, provisions and covenants herein contained, the parties hereto agree as follows:

SECTION 1. AMENDMENTS TO THE TERM LOAN AGREEMENT

1.1 Amendments to Section 4: Representations and Warranties

Section 4 of the Term Loan Agreement is hereby amended by adding a new Section 4.22 thereto as follows:

"4.22 Subordinated Indebtedness

The subordination provisions of (i) the RTC Convertible Subordinated Indenture, (ii) any Guarantee by the Borrower of the Indebtedness under the RTC Convertible Subordinated Indenture and the RTC Convertible Subordinated Notes, (iii) any Subordinated Indebtedness of the Borrower now existing or hereafter incurred or assumed by the Borrower and (iv) any Guarantee by any Subsidiary of the Borrower of any Subordinated Indebtedness of the Borrower will be enforceable against the holders thereof, and the Loans and all other monetary Obligations hereunder and all monetary obligations under the Subsidiary Guaranty will constitute "Senior Indebtedness" and "Designated Senior Indebtedness" (or any comparable terms) as defined in such provisions."



## 1.2 Amendments to Section 8: Negative Covenants

A. Section 8.1(b) of the Term Loan Agreement is hereby further amended by (i) deleting the "and" at the end of clause (xiii) thereof, (ii) relabeling clause (xiv) thereof as clause (xv) and (iii) adding a new clause (xiv) thereto as follows:

"(xiv) a Guarantee by the Borrower of RTC's obligations under the RTC Convertible Subordinated Notes provided that (a) such Guarantee is subordinated to at least the same extent as the Indebtedness under the RTC Convertible Subordinated Notes is subordinated to the Obligations of RTC under the Subsidiary Guaranty and (b) such Guarantee is otherwise on market terms for guaranties of subordinated debt instruments prevailing at or around the time such Guarantee is entered into; and".

## 1.3 Amendments to Section 11: Other Provisions

Section 11 of the Term Loan Agreement is hereby amended by adding a new Section 11.20 thereto as follows:

### "11.20 Designation as Designated Senior Indebtedness

This Agreement, the Subsidiary Guaranty, and all Loans and all other monetary Obligations hereunder and thereunder, are hereby expressly designated as "Designated Senior Indebtedness," as that term is defined in the RTC Convertible Subordinated Indenture and in any Guarantee thereof."

## SECTION 2. AMENDMENT TO THE SUBSIDIARY GUARANTY

The Subsidiary Guaranty is hereby amended by adding a new Section 4.15 thereto as follows:

### "4.15 Designation as Designated Senior Indebtedness; Incorporation of Defaults

This Guaranty, the Financing Documents, and all monetary obligations hereunder and thereunder, are hereby expressly designated as 'Designated Senior Indebtedness', as that term is defined in the 5 5/8% Indenture. The occurrence of any Default or Event of Default constitutes a default under this Guaranty."

## SECTION 3. CONDITIONS TO EFFECTIVENESS

Sections 1 and 2 of this Amendment shall become effective only upon the satisfaction of all of the following conditions precedent (the date of satisfaction of such conditions being referred to herein as the "THIRD AMENDMENT EFFECTIVE DATE"):

A. Required Lenders (as such term is defined in the Revolving Credit Agreement) shall have entered into an amendment and consent thereto that consents to this Amendment, which amendment and consent shall be in form and substance satisfactory to the Administrative Agent and Syndication Agent, and all conditions to the effectiveness thereof (other than effectiveness hereof) shall have been satisfied or waived.

B. All fees and expenses incurred by Syndication Agent and its counsel, O'Melveny & Myers LLP, in connection with the preparation, negotiation and closing of this Amendment shall have been paid by Borrower.

## SECTION 4. BORROWER'S REPRESENTATIONS AND WARRANTIES

In order to induce Lenders to enter into this Amendment and to amend the Term Loan Agreement in the manner provided herein, Borrower represents and warrants to each Lender that the following statements are true, correct and complete:

A. CORPORATE POWER AND AUTHORITY. Each Credit Party has all requisite corporate power and authority to enter into this Amendment and to carry out the transactions contemplated by, and perform its obligations under, the Term Loan Agreement as amended by this Amendment (the "AMENDED AGREEMENT").

B. AUTHORIZATION OF AGREEMENTS. The execution and delivery of this Amendment have been duly authorized by all necessary corporate action on the part of each Credit Party. The performance of the Amended Agreement has been duly authorized by all necessary corporate action on the part of each Credit Party.

C. NO CONFLICT. The execution and delivery by each Credit Party of this Amendment, and the performance by each Credit Party of the Amended Agreement do not and will not (i) violate any provision of any law or any governmental rule or regulation applicable to Borrower or any of its Subsidiaries, the Certificate or Articles of Incorporation or Bylaws of Borrower or any of its Subsidiaries or any order, judgment or decree of any court or other agency of government binding on Borrower or any of its Subsidiaries, (ii) conflict with, result in a breach of or constitute (with due notice or lapse of time or both) a default under any contractual obligation of Borrower or any of its Subsidiaries, (iii) result in or require the creation or imposition of any Lien upon any of the properties or assets of Borrower or any of its Subsidiaries (other than Liens created under any of the Loan Documents in favor of Administrative Agent on behalf of Lenders), or (iv) require any approval of stockholders or any approval or consent of any Person under any contractual obligation of Borrower or any of its Subsidiaries.

D. GOVERNMENTAL CONSENTS. The execution and delivery by each Credit Party of this Amendment, and the performance by each Credit Party of the Amended Agreement do not and will not require any registration with, consent or approval of, or notice to, or other action to, with or by, any federal, state or other governmental authority or regulatory body.

E. BINDING OBLIGATION. This Amendment and the Amended Agreement have been duly executed and delivered by each Credit Party and are the legally valid and binding obligations of each Credit Party, enforceable against each Credit Party in accordance with their respective terms, except as may be limited by bankruptcy, insolvency, reorganization, moratorium or similar laws relating to or limiting creditors' rights generally or by equitable principles relating to enforceability.

F. INCORPORATION OF REPRESENTATIONS AND WARRANTIES FROM TERM LOAN AGREEMENT. The representations and warranties contained in Section 4 of the Term Loan Agreement are and will be true, correct and complete in all material respects on and as of the Third Amendment Effective Date to the same extent as though made on and as of that date, except to the extent such representations and warranties specifically relate to an earlier date, in which case they were true, correct and complete in all material respects on and as of such earlier date.

G. ABSENCE OF DEFAULT. No event has occurred and is continuing or will result from the consummation of the transactions contemplated by this Amendment that would constitute an Event of Default.

#### SECTION 5. ACKNOWLEDGEMENT AND CONSENT

Borrower is a party to the Borrower Pledge Agreement pursuant to which Borrower has pledged certain Collateral to Administrative Agent to secure the Obligations. TRC is a party to the Subsidiary Guaranty and the Subsidiary Pledge Agreement pursuant to which TRC has (i) guarantied the Obligations and (ii) pledged certain Collateral to Administrative Agent to secure the Obligations and to secure the obligations of TRC under the Subsidiary Guaranty. TRC West, Inc. is a party to the Subsidiary Guaranty pursuant to which TRC West, Inc. has guarantied the Obligations. Total Renal Care Acquisition Corp. is a party to the Subsidiary Guaranty pursuant to which Total Renal Care Acquisition Corp. has guarantied the Obligations. Borrower, TRC, TRC West, Inc. and Total Renal Care Acquisition Corp. are collectively referred to herein as the "CREDIT SUPPORT PARTIES", and the Borrower Pledge Agreement, the Subsidiary Pledge Agreement and the Subsidiary Guaranty are collectively referred to herein as the "CREDIT SUPPORT DOCUMENTS".

Each Credit Support Party hereby acknowledges that it has reviewed the terms and provisions of the Term Loan Agreement and this Amendment and consents to the amendment of the Term Loan Agreement effected pursuant to this Amendment. Each Credit Support Party hereby confirms that each Credit Support Document to which it is a party or otherwise bound and all Collateral encumbered thereby will continue to guaranty or secure,

as the case may be, to the fullest extent possible the payment and performance of all "Guarantied Obligations" and "Secured Obligations," as the case may be (in each case as such terms are defined in the applicable Credit Support Document), including without limitation the payment and performance of all such "Guarantied Obligations" and "Secured Obligations," as the case may be, in respect of the Obligations of Borrower now or hereafter existing under or in respect of the Amended Agreement and the Notes defined therein.

Each Credit Support Party acknowledges and agrees that any of the Credit Support Documents to which it is a party or otherwise bound shall continue in full force and effect and that all of its obligations thereunder shall be valid and enforceable and shall not be impaired or limited by the execution or effectiveness of this Amendment. Each Credit Support Party represents and warrants that all representations and warranties contained in the Amended Agreement and the Credit Support Documents to which it is a party or otherwise bound are true, correct and complete in all material respects on and as of the Third Amendment Effective Date to the same extent as though made on and as of that date, except to the extent such representations and warranties specifically relate to an earlier date, in which case they were true, correct and complete in all material respects on and as of such earlier date.

Each Credit Support Party acknowledges and agrees that (i) notwithstanding the conditions to effectiveness set forth in this Amendment, such Credit Support Party is not required by the terms of the Term Loan Agreement or any other Loan Document to consent to the amendments to the Term Loan Agreement effected pursuant to this Amendment and (ii) nothing in the Term Loan Agreement, this Amendment or any other Loan Document shall be deemed to require the consent of such Credit Support Party to any future amendments to the Term Loan Agreement.

#### SECTION 6. MISCELLANEOUS

##### A. REFERENCE TO AND EFFECT ON THE TERM LOAN AGREEMENT AND THE OTHER LOAN DOCUMENTS.

(i) On and after the Third Amendment Effective Date, each reference in the Term Loan Agreement to "this Agreement", "hereunder", "hereof", "herein" or words of like import referring to the Term Loan Agreement, and each reference in the other Loan Documents to the "Term Loan Agreement", "thereunder", "thereof" or words of like import referring to the Term Loan Agreement shall mean and be a reference to the Amended Agreement.

(ii) On and after the Third Amendment Effective Date, each reference in the Subsidiary Guaranty to "this Agreement", "hereunder", "hereof", "herein" or words of like import referring to the Subsidiary Guaranty and each reference in the other Loan Documents to the "Subsidiary Guaranty", "thereunder", "thereof" or words of like import referring to the Subsidiary Guaranty shall mean and be a reference to the Subsidiary Guaranty as amended by this Amendment.

(iii) Except as specifically amended by this Amendment, the Term Loan Agreement and the other Loan Documents shall remain in full force and effect and are hereby ratified and confirmed.

(iv) The execution, delivery and performance of this Amendment shall not, except as expressly provided herein, constitute a waiver of any provision of, or operate as a waiver of any right, power or remedy of Administrative Agent or any Lender under, the Term Loan Agreement or any of the other Loan Documents.

B. FEES AND EXPENSES. Borrower acknowledges that all costs, fees and expenses as described in Section 11.5 of the Term Loan Agreement incurred by Administrative Agent, Syndication Agent, Co-Arrangers, and Special Counsel, with respect to this Amendment and the documents and transactions contemplated hereby shall be for the account of Borrower.

C. HEADINGS. Section and subsection headings in this Amendment are included herein for convenience of reference only and shall not constitute a part of this Amendment for any other purpose or be given any substantive effect.

D. APPLICABLE LAW. THIS AMENDMENT AND THE RIGHTS AND OBLIGATIONS OF THE PARTIES HEREUNDER SHALL BE GOVERNED BY, AND SHALL BE CONSTRUED AND ENFORCED IN ACCORDANCE WITH, THE INTERNAL LAWS OF THE STATE OF NEW YORK (INCLUDING WITHOUT LIMITATION SECTION 5-1401 OF THE GENERAL OBLIGATIONS LAW OF THE STATE OF NEW YORK), WITHOUT REGARD TO CONFLICTS OF LAWS PRINCIPLES.

E. COUNTERPARTS; EFFECTIVENESS. This Amendment may be executed in any number of counterparts and by different parties hereto in separate counterparts, each of which when so executed and delivered shall be deemed an original, but all such counterparts together shall constitute but one and the same instrument; signature pages may be detached from multiple separate counterparts and attached to a single counterpart so that all signature pages are physically attached to the same document. This Amendment (other than the provisions of Sections 1 and 2 hereof, the effectiveness of which is governed by Section 3 hereof) shall become effective upon the execution of a counterpart hereof by Borrower, Required Lenders, Administrative Agent, and each of the Credit Support Parties and receipt by Borrower and Administrative Agent of written or telephonic notification of such execution and authorization of delivery thereof.

[Remainder of page intentionally left blank]

IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first written above.

BORROWER: TOTAL RENAL CARE HOLDINGS, INC.  
By: \_\_\_\_\_  
Title: \_\_\_\_\_

CREDIT SUPPORT PARTIES: TOTAL RENAL CARE, INC., (for  
purposes of Sections 2 and 5 only)  
as a Credit Support Party

By: \_\_\_\_\_  
Title: \_\_\_\_\_

TRC WEST, INC., (for purposes of  
Sections 2 and 5 only) as a Credit  
Support Party

By: \_\_\_\_\_  
Title: \_\_\_\_\_

TOTAL RENAL CARE ACQUISITION CORP.,  
(for purposes of Sections 2 and 5  
only) as a Credit Support Party

By: \_\_\_\_\_  
Title: \_\_\_\_\_

AGENTS: THE BANK OF NEW YORK, Individually  
as Administrative Agent, and  
Collateral Agent

By: \_\_\_\_\_  
Title: \_\_\_\_\_

DLJ CAPITAL FUNDING, INC.,  
Individually and as Syndication  
Agent

By: \_\_\_\_\_  
Title: \_\_\_\_\_

LENDERS:

BDC FINANCE, LLC

By: \_\_\_\_\_  
Title: \_\_\_\_\_

CITIBANK, N.A.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

CONTINENTAL ASSURANCE COMPANY  
Separate Account (E)

By: TCW Asset Management Company, as  
Attorney-In-Fact, as Assignee

By: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Title: \_\_\_\_\_

DEBT STRATEGIES FUND, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

DEEPROCK & COMPANY

By: Eaton Vance Management as  
Investment Advisor

By: \_\_\_\_\_  
Title: \_\_\_\_\_

FRANKLIN FLOATING RATE TRUST

By: \_\_\_\_\_  
Title: \_\_\_\_\_

KZH HOLDING CORPORATION III

By: \_\_\_\_\_  
Title: \_\_\_\_\_

KZH--CRESCENT CORPORATION

By: \_\_\_\_\_  
Title: \_\_\_\_\_

KZH--SOLEIL CORPORATION

By: \_\_\_\_\_  
Title: \_\_\_\_\_

LEHMAN COMMERCIAL PAPER INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

MERRILL LYNCH SENIOR FLOATING RATE  
FUND, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

MORGAN STANLEY SENIOR FUNDING, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

OCTAGON CREDIT INVESTORS LOAN  
PORTFOLIO (a unit of The Chase  
Manhattan Bank)

By: \_\_\_\_\_  
Title: \_\_\_\_\_

ORIX USA CORP.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

PARIBAS CAPITAL FUNDING LLC

By: \_\_\_\_\_  
Title: \_\_\_\_\_

PILGRIM AMERICA PRIME RATE TRUST

By: \_\_\_\_\_  
Title: \_\_\_\_\_



SENIOR DEBT PORTFOLIO

By: Boston Management and Research,  
as Investment Advisor

By: \_\_\_\_\_  
Title: \_\_\_\_\_

SENIOR HIGH INCOME PORTFOLIO, INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

T. ROWE PRICE HIGH YIELD FUND INC.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

VAN KAMPEN AMERICAN CAPITAL PRIME  
RATE INCOME TRUST

By: \_\_\_\_\_  
Title: \_\_\_\_\_

MERRILL LYNCH PRIME RATE PORTFOLIO

By: Merrill Lynch Asset Management,  
L.P., as Investment Advisor

By: \_\_\_\_\_  
Title: \_\_\_\_\_

FIRST SUPPLEMENTAL INDENTURE (this "First Supplemental Indenture") dated as of February 27, 1998, among Renal Treatment Centers, Inc., a Delaware corporation (the "Company"), Total Renal Care Holdings, Inc., a Delaware corporation ("TRCH"), and PNC Bank, National Association, as trustee (the "Trustee"), under the Indenture (the "Indenture") dated as of June 12, 1996, between the Company and the Trustee.

WHEREAS pursuant to an Agreement and Plan of Merger dated as of November 18, 1997 (the "Merger Agreement"), among TRCH, Nevada Acquisition Corp., a Delaware corporation and a wholly owned subsidiary of TRCH ("Merger Sub") and the Company, Merger Sub merged with and into the Company (the "Merger") and the Company continued as the surviving corporation and thereupon became a wholly owned subsidiary of TRCH;

WHEREAS pursuant to the Merger Agreement, each outstanding share of common stock, par value \$0.01 per share, of the Company ("RTC Common Stock") will be converted into 1.335 shares of common stock, par value \$0.001 per share, of TRCH ("TRCH Common Stock");

WHEREAS in connection with the Merger and the conversion of RTC Common Stock into TRCH Common Stock, TRCH is required to execute and deliver to the Trustee a supplemental indenture pursuant to Sections 15.6 and 16.5 of the Indenture;

WHEREAS Section 11.1 of the Indenture provides that, without the consent of the Noteholders, the Company, when authorized by a resolution of its Board of Directors, and the Trustee may enter into indentures supplemental to the Indenture for the purpose of, among other things, making provision with respect to adjustments to the conversion rights of holders pursuant to the requirements of Section 15.6 and the repurchase obligations of the Company pursuant to the requirements of Section 16.5;

WHEREAS the entry into this First Supplemental Indenture by the parties hereto is in all respects authorized by the provisions of the Indenture; and

WHEREAS all things necessary to make this First Supplemental Indenture a valid indenture and agreement according to its terms have been done;

NOW THEREFORE, TRCH hereby covenants and agrees with the Company and the Trustee for the benefit of the present and future holders of the Notes as follows:

#### ARTICLE I

##### SECTION 1.01 Conversion Right. The holder of each Note outstanding

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as of the date the Merger is consummated shall have the right, during the period such Note shall be convertible as specified in Section 15.1 of the Indenture, to convert such Note into shares of TRCH Common Stock equal to 1.335 times the number of shares of RTC Common Stock such holder would have had the right to receive upon conversion immediately prior to the date of the consummation of the Merger.

##### SECTION 1.02 Antidilution Adjustments. The conversion price in

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effect at any time shall be subject to adjustment as set forth in Section 15.5 of the Indenture.

#### ARTICLE II

##### SECTION 2.01 Amendment to Definition of "Common Stock". The

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definition of "Common Stock" set forth in Section 1.1 of the Indenture is hereby amended by deleting it in its entirety and replacing it with the following:

"The term "Common Stock" shall mean any stock of any class of TRCH which has no preference in respect of dividends or of amounts payable in the event of any voluntary or involuntary liquidation, dissolution or winding up of TRCH and which is not subject to redemption by TRCH. Subject to the provisions of Section 15.6, however, shares issuable on conversion of Notes shall include only

shares of the class designated as common stock of TRCH as of February 27, 1998, or shares of any class or classes resulting from any reclassification or reclassifications hereof and which have no preference in respect of dividends or of amounts payable in the event of any voluntary or involuntary liquidation, dissolution or winding up of TRCH and which are not subject to redemption by TRCH; provided that

if at any time there shall be more than one such resulting class, the shares of each such class then so issuable shall be substantially in the proportion which the total number of shares of such class resulting from all such reclassifications bears to the total number of shares of all such classes resulting from all such reclassifications."

SECTION 2.02 Definition of "TRCH". The following definition shall be added to Section 1.1 of the Indenture:

"TRCH: The term "TRCH" shall mean Total Renal Care Holdings, Inc., a Delaware corporation."

SECTION 2.03 Amendments to Article XV. Article XV is hereby amended such that each reference therein to "the Company" shall be deemed to read "TRCH" and each reference therein to the "Board of Directors" shall mean the Board of Directors of TRCH.

SECTION 2.04 Amendment to Section 16.4. Pursuant to Section 16.5 of the Indenture, Section 16.4 is hereby amended such that each reference therein to the Company shall be deemed to read "TRCH".

### ARTICLE III

SECTION 3.01 First Supplemental Indenture. The Trustee accepts the provisions of this First Supplemental Indenture upon the terms and conditions set forth in the Indenture as amended by this First Supplemental Indenture.

SECTION 3.02 Other Terms of Indenture. Except insofar as herein

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otherwise expressly provided, all the provisions, terms and conditions of the Indenture are in all respects ratified and confirmed and shall remain in full force and effect.

SECTION 3.03 Definitions. Capitalized terms used herein and not

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defined herein have the meanings ascribed to such terms in the Indenture unless the context of this First Supplemental Indenture otherwise requires.

SECTION 3.04 Governing Law. This First Supplemental Indenture shall

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be deemed to be a contract made under the laws of New York, and for all purposes shall be construed in accordance with, the laws of New York.

SECTION 3.05 Counterparts. This First Supplemental Indenture may be

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executed in any number of counterparts, each of which shall be an original, but such counterparts shall together constitute but one and the same instrument.

IN WITNESS WHEREOF, the parties hereto have caused this First Supplemental Indenture to be duly executed by their respective authorized officers as of the date first written above.

TOTAL RENAL CARE HOLDINGS, INC.,

by

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Name:  
Title:

Attest:

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Name:

RENAL TREATMENT CENTERS, INC.,

by

-----  
Name:  
Title:

Attest:

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Name:

PNC BANK, NATIONAL ASSOCIATION  
as Trustee,

by

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Name:  
Title:

Attest:

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Name:

## EXECUTION COPY

SECOND SUPPLEMENTAL INDENTURE (this "Second Supplemental Indenture") dated as of March 31, 1998, among Renal Treatment Centers, Inc., a Delaware corporation (the "Company"), Total Renal Care Holdings, Inc., a Delaware corporation ("TRCH"), and PNC Bank, National Association, as trustee (the "Trustee"), under the Indenture (the "Indenture") dated as of June 12, 1996, between the Company and the Trustee, as amended by that certain First Supplemental Indenture, dated as of February 27, 1998, among the Company, TRCH and the Trustee.

WHEREAS pursuant to an Agreement and Plan of Merger dated as of November 18, 1997 (the "Merger Agreement"), among TRCH, Nevada Acquisition Corp., a Delaware corporation and a wholly owned subsidiary of TRCH ("Merger Sub") and the Company, Merger Sub merged with and into the Company (the "Merger") and the Company continued as the surviving corporation and thereupon became a wholly owned subsidiary of TRCH;

WHEREAS the Boards of Directors of the Company and TRCH have determined that it is in the best interests of the Company and TRCH, on the one hand, and the noteholders, on the other hand, to make TRCH a guarantor of the obligations of the Company under the Indenture;

WHEREAS TRCH, in furtherance of the foresaid determinations, as guarantor, will enter into a guaranty in the form attached hereto as Exhibit A (the "Guaranty") in favor of the Trustee for the benefit of the Noteholders;

WHEREAS Section 11.1(d) of the Indenture provides that, without the consent of the Noteholders, the Company, when authorized by a resolution of its Board of Directors, and the Trustee may enter into indentures supplemental to the Indenture in order to, among other things, add such further covenants, restrictions or conditions as the Company's Board of Directors and the Trustee shall consider to be for the benefit of the holders of the Notes;

WHEREAS the entry into this Second Supplemental Indenture by the parties hereto is in all respects authorized by the provisions of the Indenture; and

WHEREAS all things necessary to make this Second Supplemental Indenture a valid indenture and agreement according to its terms have been done;

NOW THEREFORE, TRCH hereby covenants and agrees with the Company and the Trustee for the benefit of the present and future holders of the Notes as follows:

## ARTICLE I

SECTION 1.01 Guaranty of the Notes by TRCH. For value received and pursuant to the Guaranty dated March 31, 1998 in favor of the Trustee for the benefit of the Noteholders, TRCH guarantees (a) the due and punctual payment of the principal of, and premium, if any, and interest on each Note, when and as the same shall become due and payable, subject to any applicable grace period, whether at maturity, by acceleration or otherwise, the due and punctual payment of interest on the overdue principal of, and premium, if any, and interest on the Notes, to the extent lawful, and the due and punctual performance of all other Obligations (as defined in the Guaranty) of Company to the Noteholders or the Trustee all in accordance with the terms of such Note and the Indenture, subject, however, to the limitations set forth in the Guaranty, and (ii) in the case of any extension of time of payment or renewal of any Notes or any of such other Obligations, that the same will be promptly paid in full when due or performed in accordance with the terms of the extension or renewal, at stated maturity, by acceleration or otherwise. TRCH hereby agrees that its obligations under the Guaranty shall be absolute and unconditional, irrespective of, and shall be unaffected by, any invalidity, irregularity or unenforceability of any



such Note or the Indenture, any failure to enforce the provisions of any such Note or the Indenture, any waiver, modification or indulgence granted to Company with respect thereto by the Noteholder of such Note or the Trustee, or any other circumstances which may otherwise constitute a legal or equitable discharge of a surety or Guarantor.

SECTION 1.02 Effectiveness of the Guaranty. TRCH agrees that the Guaranty set forth in Section 1.02 above shall be and remain in full force and effect notwithstanding any failure to endorse on each Note a notation of such Guaranty and that each Note shall be entitled to the full benefit of the Guaranty whether or not the Guaranty is notated thereon.

## ARTICLE II

SECTION 2.01 Definition of "Guaranty". The following definition shall be added to Section 1.1 of the Indenture:

"Guaranty: The term "Guaranty" shall mean a Guaranty in the form attached hereto as Exhibit A, in favor of and for the benefit of the Trustee, as representative of the Noteholders.

SECTION 2.02 Amendment to Section 7.1. Section 7.1 of the Indenture is hereby amended by adding a new sentence after the second complete sentence of that section as follows:

"In addition, without limiting the foregoing provisions, upon the effectiveness of such acceleration of the principal of all the Notes and the interest accrued thereon, the Trustee shall promptly make a demand for payment on the Notes under the Guaranty not discharged."

SECTION 2.03 Amendment to Section 14.1. Section 14.1 of the Indenture is hereby amended by adding a new sentence to the end of that section as follows:

"Notwithstanding the foregoing, the Trustee may seek recourse for the payment of the principal of or premium, if any, or interest on any Note, or for any claim based thereon or otherwise in respect thereof or for Obligations (as defined in the Guaranty) of the Company against TRCH under the Guaranty in accordance with the provisions of Article VII and the Guaranty."

## ARTICLE III

SECTION 3.01 Second Supplemental Indenture. The Trustee accepts the provisions of this Second Supplemental Indenture upon the terms and conditions set forth in the Indenture as amended by this Second Supplemental Indenture.

SECTION 3.02 Other Terms of Indenture. Except insofar as herein otherwise expressly provided, all the provisions, terms and conditions of the Indenture are in all respects ratified and confirmed and shall remain in full force and effect.

SECTION 3.03 Definitions. Capitalized terms used herein and not defined herein have the meanings ascribed to such terms in the Indenture unless the context of this Second Supplemental Indenture otherwise requires.

SECTION 3.04 Governing Law. This Second Supplemental Indenture shall be deemed to be a contract made under the laws of New York, and for all purposes shall be construed in accordance with, the laws of New York.

SECTION 3.05 Counterparts. This Second Supplemental Indenture may be executed in any number of counterparts, each of which shall be an original, but such counterparts shall together constitute but one and the same instrument.

IN WITNESS WHEREOF, the parties hereto have caused this Second Supplemental Indenture to be duly executed by their respective authorized officers as of the date first written above.

TOTAL RENAL CARE HOLDINGS, INC.,

by

-----  
Name:

Title:

Attest:

-----  
Name:

RENAL TREATMENT CENTERS, INC.,

by

-----  
Name:

Title:

Attest:

-----  
Name:

PNC BANK, NATIONAL ASSOCIATION  
as Trustee,

by

-----  
Name:

Title:

Attest:

-----  
Name:

## EXHIBIT A

### GUARANTY

This Guaranty (this "Guaranty") is entered into as of March 31, 1998 by Total Renal Care Holdings, Inc., a Delaware corporation ("Guarantor"), in favor of PNC Bank, National Association, as Trustee ("Trustee") for the benefit of the noteholders ("Noteholders") under that certain Indenture, dated as of June 12, 1996, between Renal Treatment Centers, Inc., a Delaware corporation and wholly owned subsidiary of Guarantor ("Company"), and Trustee, as amended by that certain First Supplemental Indenture, dated as of February 27, 1998, between Company, Guarantor and Trustee (as amended, supplemented or otherwise modified from time to time, the "Indenture") with respect to Company's 5 5/8% Convertible Subordinated Notes due 2006 (the "Notes"). Unless otherwise defined herein, capitalized terms used in this Guaranty shall have the meanings assigned to such terms in the Indenture.

### RECITALS

A. Company became a wholly owned subsidiary of Guarantor pursuant to that certain Agreement and Plan of Merger by and among Guarantor, Nevada Acquisition Corp., a Delaware corporation, and Company, dated as of November 18, 1997 (the "Merger").

B. Guarantor has determined that it is in its best interest irrevocably and unconditionally to guaranty the Notes.

Now, therefore, based upon the foregoing and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Guarantor hereby agrees as follows:

### SECTION 1

#### DEFINITIONS

1.1 Certain Defined Terms. As used in this Guaranty, the following terms shall have the following meanings unless the context otherwise requires:

"Additional Interest" means additional interest on the Notes pursuant to Section 2.3 of the Indenture which Company and Guarantor, jointly and severally, hereby agree to pay to the Noteholders.

"Credit Facilities" means, collectively, (i) Guarantor's \$800,000,000 Revolving Credit Agreement, dated as of October 24, 1997 with DLJ Capital Funding, Inc., as Syndication Agent, First Union National Bank, as Documentation Agent, The Bank of New York, as Administrative Agent, BNY Capital Markets, Inc. and Donaldson, Lufkin & Jenrette Securities Corporation, as Co-Arrangers, and the various lenders party thereto, together with the promissory notes issued thereunder and the other documents related thereto, and (ii) Guarantor's \$250,000,000 Term Loan Agreement, dated as of October 24, 1997, with DLJ Capital Funding, Inc., as Syndication Agent, The Bank of New York, as Administrative Agent, BNY Capital Markets, Inc. and Donaldson, Lufkin & Jenrette Securities Corporation, as Co-Arrangers, and the various lenders party thereto, together with the promissory notes issued thereunder and the other documents related thereto, in each case as such agreements may be amended (including any amendment and restatement thereof), supplemented or otherwise modified from time to time, including any agreements extending the maturity of, refinancing, replacing or otherwise restructuring (including increasing the amount of available borrowings thereunder or adding subsidiaries of Guarantor and/or Company as additional borrowers or guarantors thereunder) all or any portion of the Indebtedness and other Obligations under such agreements and whether by the same or any other agent, lender or group of lenders.

"Designated Senior Indebtedness" means any Indebtedness under either of the Credit Facilities and any other Indebtedness in an original principal amount of at least \$50 million, provided that by its terms such Indebtedness expressly provides that it is "Designated Senior Indebtedness" for purposes of this Guaranty.

"Indebtedness" means (without duplication), with respect to any Person, any obligation at any time outstanding, secured or unsecured, contingent or otherwise, which is for borrowed money (whether or not the recourse of the lender is to the whole of the assets of such Person or only to a portion thereof), or evidenced by bonds, notes, debentures or similar instruments or representing the balance deferred and unpaid of the purchase price of any property (excluding, without limitation, any balance that constitutes accounts payable or trade payables, and other accrued liabilities arising in the ordinary course of business) if and to the extent any of the foregoing indebtedness would appear as a liability upon a balance sheet of such Person prepared in accordance with generally accepted accounting principles ("GAAP"), and shall also include, to the extent not otherwise included, (i) any obligations secured by a lien to which the property or assets owned or held by such Person is subject, whether or not the obligation or obligations secured thereby shall have been assumed, to the extent of the fair market value of such property or assets, (ii) guarantees of items of other Persons which would be included within this definition for such other Persons (whether or not such items would appear upon the balance sheet of the guarantor), to the extent of the amount of the Indebtedness so guaranteed, and (iii) all obligations for the reimbursement of any obligor on any letter of credit, banker's acceptance or similar credit transaction. The amount of Indebtedness of any Person at any date shall be the outstanding balance at such date of all unconditional obligations as described above and, with respect to contingent obligations, the maximum liability upon the occurrence of the contingency giving rise to the obligations; provided, that (i) the amount outstanding at any time of any Indebtedness issued with original issue discount is the principal amount of such Indebtedness less the remaining unamortized portion of the original issue discount of such Indebtedness at such time as determined in conformity with GAAP and (ii) Indebtedness shall not include any liability for federal, state, local or other taxes. Notwithstanding any other provision of the foregoing definition, any trade payable arising from the purchase of goods or materials or for the services obtained in the ordinary course of business shall not be deemed to be "Indebtedness." Furthermore, guarantees of (or obligations with respect to letters of credit supporting) Indebtedness otherwise included in the determination of such amount shall not also be included.

"Non-Payment Event of Default" means any event (other than a Payment Default) the occurrence of which entitles one or more Persons to accelerate the maturity of any Designated Senior Indebtedness.

"Obligations" means, with respect to any Indebtedness, any principal, premium, interest, penalties, fees, indemnifications, reimbursements, damages and other expenses payable under the documentation governing such Indebtedness.

"Payment Default" means any default, whether or not any requirement for the giving of notice, the lapse of time or both, or any other condition to such default becoming an event of default has occurred, in the payment of principal of or premium, if any, or interest on or any other amount payable in connection with any Designated Senior Indebtedness.

"Person" means any individual, corporation, company (including any limited liability company), partnership, joint venture, trust, unincorporated organization, government or any agency or political subdivision thereof or any other entity.

"Senior Indebtedness," as to Guarantor, means the principal of and premium, if any, and interest on, and any and all other fees, expense reimbursement obligations and all other Obligations and amounts due pursuant to the terms of all agreements, documents and instruments providing for, creating, securing or evidencing or otherwise entered into in connection with (a) all Indebtedness of Guarantor owed to lenders or agents under either of the Credit Facilities, (b) all obligations of Guarantor to reimburse any bank or other person in respect of amounts paid under letters of credit, acceptances or other similar instruments and all obligations of Guarantor with respect to guarantees of such reimbursement obligations, (c) all other Indebtedness of Guarantor which does not provide that it is to be ranked *pari passu* with or subordinate to the Guaranty and (d) all deferrals, renewals,

refinancings, extensions and refundings of, and amendments, modifications and supplements to, any of the Senior Indebtedness described above. Notwithstanding anything to the contrary in the foregoing, Senior Indebtedness will not include (i) Indebtedness of Guarantor to any of its Subsidiaries, or to any Affiliate of Guarantor or any of such Affiliate's Subsidiaries, (ii) Indebtedness represented by the Guaranty, (iii) any Indebtedness which by the express terms of the agreement or instrument creating, evidencing or governing the same is junior or subordinate in right of payment to any item of Senior Indebtedness, (iv) any trade payable arising from the purchase of goods or materials or for services obtained in the ordinary course of business, and (v) any Indebtedness to or guaranteed on behalf of, any stockholders, director, officer or employee of Guarantor or any Subsidiary of Guarantor.

## SECTION 2

### THE GUARANTY

#### 2.1 Guaranty.

(a) Subject to the provisions hereof, Guarantor hereby unconditionally guarantees in favor of the Trustee for benefit of the Noteholders, (i) the due and punctual payment of the principal of, and premium, if any, and interest on each Note, when and as the same shall become due and payable, subject to any applicable grace period, whether at maturity, by acceleration or otherwise, the due and punctual payment of interest on the overdue principal of, and premium, if any, and interest on the Notes, to the extent lawful, and the due and punctual performance of all other Obligations of Company to the Noteholders or the Trustee all in accordance with the terms of such Note and the Indenture, subject, however, to the limitations set forth in Section 2.2, and (ii) in the case of any extension of time of payment or renewal of any Notes or any of such other Obligations, that the same will be promptly paid in full when due or performed in accordance with the terms of the extension or renewal, at stated maturity, by acceleration or otherwise. Guarantor hereby agrees that its obligations thereunder and hereunder shall be absolute and unconditional, irrespective of, and shall be unaffected by, any invalidity, irregularity or unenforceability of any such Note or the Indenture, any failure to enforce the provisions of any such Note or the Indenture, any waiver, modification or indulgence granted to Company with respect thereto by the Noteholder of such Note or the Trustee, or any other circumstances which may otherwise constitute a legal or equitable discharge of a surety or Guarantor.

(b) Guarantor hereby waives diligence, presentment, demand for payment, filing of claims with a court in the event of merger or bankruptcy of Company, any right to require a proceeding first against Company, protest or notice with respect to any such Note or the Indebtedness evidenced thereby and all demands whatsoever, and covenants that this Guaranty will not be discharged as to any such Note except by payment in full of the principal thereof, premium if any, and interest thereon and as provided in Section 13.1 of the Indenture. Guarantor further agrees that, as between Guarantor, on the one hand, and the Noteholders and the Trustee, on the other hand, (i) the maturity of the Obligations guaranteed hereby may be accelerated as provided in Article 7 of the Indenture for the purposes of this Guaranty, notwithstanding any stay, injunction or other prohibition preventing such acceleration in respect of the Obligations guaranteed hereby, and (ii) in the event of any declaration of acceleration of such Obligations as provided in Article 7 of the Indenture, such Obligations (whether or not due and payable) shall forthwith become due and payable by Guarantor for the purpose of this Guaranty. In addition, without limiting the foregoing provisions, upon the effectiveness of an acceleration under Article 7 of the Indenture, the Trustee shall promptly make a demand for payment on the Notes under the Guaranty provided for herein and not discharged.

2.2 Effectiveness of the Guaranty. Guarantor agrees that this Guaranty shall be and remain in full force and effect notwithstanding any failure to endorse on each Note a notation of such Guaranty and that each Note shall be entitled to the full benefit of the Guaranty whether or not the Guaranty is notated thereon.

2.3 Limitation of Guaranty. Notwithstanding any term or provision of the Indenture to the contrary, the maximum aggregate amount of the obligations guaranteed hereunder by Guarantor shall not exceed the maximum amount that can be guaranteed hereunder by Guarantor without rendering the Guaranty, as it relates to Guarantor, voidable under applicable law relating to fraudulent conveyance or fraudulent transfer or similar laws affecting the rights of creditors generally.

2.4 Guaranty Obligations Subordinated to Guarantor Senior Indebtedness.

(a) Guarantor hereby covenants and agrees that, to the extent and in the manner set forth herein, the Indebtedness represented by the Guaranty and the payment of the principal of, premium, if any, and interest on the Notes pursuant to the Guaranty by Guarantor are hereby expressly made subordinate and subject in right of payment as provided herein to the prior indefeasible payment and satisfaction in full in cash of all Senior Indebtedness.

(b) The holders of Senior Indebtedness (including, without limitation, Designated Senior Indebtedness) shall have the right to rely on this Section 2.4 and the following Section 2.4 through Section 2.12, and such provisions are made for the benefit of the holders of Senior Indebtedness; and such holders are made obligees hereunder and they or each of them may enforce such provisions, and no amendment or modification of the provisions contained herein shall diminish the rights of such holders unless such holders have agreed in writing thereto.

2.5 Payment Over of Proceeds upon Dissolution, etc., of Guarantor. In the event of (x) any insolvency or bankruptcy case or proceeding, or any receivership, arrangement, reorganization, liquidation, dissolution or other similar case or proceeding in connection therewith whether or not involving insolvency or bankruptcy, relative to Guarantor or to its creditors, as such, or to its assets, whether voluntary or involuntary, or (y) any general assignment for the benefit of creditors or other marshaling of assets or liabilities of Guarantor (except in connection with the merger or consolidation of Guarantor or its liquidation or dissolution following the transfer of all or substantially all of its assets, upon the terms and conditions that would be permitted under Article 12 of the Indenture if references to "Company" were to Guarantor) (all of the foregoing referred to herein individually as a "Guarantor Bankruptcy Proceeding" and collectively as "Guarantor Bankruptcy Proceedings"), then and in any such event:

i. the holders of all Senior Indebtedness shall be entitled to receive payment and satisfaction in full in cash of all amounts due on or in respect of all such Senior Indebtedness (including any interest accruing after the commencement of any such Guarantor Bankruptcy Proceeding whether or not such interest is an allowable claim enforceable against Company in any such proceeding) before the Noteholders are entitled to receive or retain, pursuant to this Guaranty, any payment or distribution of any kind by Guarantor on account of this Guaranty;

ii. any payment or distribution of assets of Guarantor of any kind or character, whether in cash, property or securities, by set-off or otherwise, to which the Noteholders or the Trustee would be entitled but for the subordination provisions hereof shall be paid by the liquidating trustee or agent or other Person making such payment or distribution, whether a trustee in bankruptcy, a receiver or liquidating trustee or otherwise, directly to the holders of Senior Indebtedness or their representative or representatives or to the trustee or trustees under any indenture under which any instruments evidencing any of such Senior Indebtedness may have been issued, ratably according to the aggregate amounts remaining unpaid on account of such Senior Indebtedness held or represented by each, to the extent necessary to make payment in full in cash of all such Senior Indebtedness remaining unpaid, after giving effect to any concurrent payment or distribution, or provision therefor, to the holders of such Senior Indebtedness;

iii. in the event that, notwithstanding the foregoing provisions of this Section 2.5, the Trustee or the Noteholder of any Note shall have received any payment or distribution of assets of Guarantor of any kind or character, whether in cash, property or securities, including, without limitation, by way of set-off or otherwise, in respect of this Guaranty before all Senior Indebtedness is paid and satisfied in full in cash,

then such payment or distribution shall be held by the recipient in trust for the benefit of holders of such Senior Indebtedness and shall be immediately paid over or delivered to the holders of such Senior Indebtedness or their representative or representatives to the extent necessary to make payment in full in cash of all such Senior Indebtedness remaining unpaid after giving effect to any concurrent payment or distribution to or for the holders of such Senior Indebtedness; and

iv. the consolidation of Guarantor with, or the merger of Guarantor with or into, another Person or the liquidation or dissolution of Guarantor following the conveyance, transfer or lease of its properties and assets substantially as an entirety to another Person upon the terms and conditions set forth herein shall not be deemed a dissolution, winding-up, liquidation, reorganization, assignment for the benefit of creditors or marshaling of assets and liabilities of such Guarantor for, as would be applicable as if references to "Company" were to Guarantor, the purposes of Article 12 of the Indenture if the Person formed by such consolidation or the surviving entity of such merger or the Person which acquires by conveyance, transfer or lease such properties and assets substantially as an entirety, as the case may be, shall, as a part of such consolidation, merger, conveyance, transfer or lease, comply with the conditions set forth in such Article 12 of the Indenture, as would be applicable as if references to "Company" were to Guarantor.

## 2.6 Suspension of Guaranty Obligations When Senior Indebtedness in Default.

(a) Unless Section 2.5 hereof shall be applicable, after the occurrence of a Payment Default with respect to any Designated Senior Indebtedness which constitutes Senior Indebtedness, no payment or distribution of any kind or character of Guarantor (including, without limitation, cash, property and any payment or distribution which may be payable or deliverable by reason of the payment of any other Indebtedness of Guarantor being subordinated to its Obligations herein) may be made by or on behalf of Guarantor, including, without limitation, by way of set-off or otherwise, for or on account hereof, and neither the Trustee nor any Noteholder shall take or receive from Guarantor, directly or indirectly in any manner, payment in respect of all or any portion of its Obligations hereof commencing on the date of receipt by the Trustee of written notice from any representative of the holders of any Designated Senior Indebtedness which constitutes Senior Indebtedness (each, a "Guarantor Representative") of such Payment Default, and in any such event, such prohibition shall continue until such Payment Default is cured, waived in writing or ceases to exist. At such time as the prohibition set forth in the preceding sentence shall no longer be in effect, subject to the provisions of the preceding and following paragraph, Guarantor shall resume making any and all required payments in respect hereof, including any missed payments.

(b) Unless Section 2.5 hereof shall be applicable, upon the occurrence of a Non-Payment Event of Default on Designated Senior Indebtedness, no payment or distribution of any kind or character (including, without limitation, cash, property and any payment or distribution which may be payable or deliverable by reason of the payment of any other Indebtedness of Guarantor being subordinated to its Obligations herein) shall be made by Guarantor, including, without limitation, by way of set-off or otherwise, for or on account of any of its Obligations herein, and neither the Trustee nor any Noteholder shall take or receive from Guarantor, directly or indirectly in any manner, payment in respect of all or any portion of its obligations on its Guaranty for a period (a "Guaranty Payment Blockage Period") commencing on the date of receipt by the Trustee of written notice from any Guarantor Representative of such Non-Payment Event of Default, unless and until (subject to any blockage of payments that may then be in effect under the preceding paragraphs), the earlier of: (x) the date that such Non-Payment Event of Default shall have been cured or waived in writing or shall have ceased to exist or such Designated Senior Indebtedness shall have been paid in full in cash or (y) the date that such Guaranty Payment Blockage Period shall have been terminated by written notice to Guarantor or the Trustee from the applicable Guarantor Representative, after which, in the case of clause (x) or (y), Guarantor shall resume making any and all required payments in respect of its Obligations herein, including any missed payments. Any number of additional Guaranty Payment Blockage Periods may be commenced during any Guaranty Payment Blockage Period.

(c) In the event that, notwithstanding the foregoing, the Trustee or any Noteholder shall have received any payment or distribution from Guarantor prohibited by the foregoing provisions of this Section 2.6, then and in

such event such payment or distribution shall be held in trust for the benefit of and shall be paid over and delivered forthwith to the holders of the Senior Indebtedness or their representative or representatives for distribution to the holders of Senior Indebtedness or, if no amounts are then due in respect of Senior Indebtedness, promptly returned to Guarantor, or otherwise as a court of competent jurisdiction shall direct.

#### 2.7 Subrogation to Rights of Noteholders of Senior Indebtedness.

(a) Upon the payment in full in cash of all Senior Indebtedness, the Noteholders shall be subrogated to the rights of the holders of such Senior Indebtedness to receive payments and distributions of cash, property and securities of Guarantor made on such Senior Indebtedness until all amounts due to be paid hereunder shall be paid in full. For purposes of such subrogation, no payments or distributions to holders of Senior Indebtedness of any cash, property or securities to which Noteholders or the Trustee would be entitled except for the provisions hereof, and no payments over pursuant to the provisions hereof to holders of Senior Indebtedness by Noteholders or the Trustee, shall, as among Guarantor, its creditors other than holders of Senior Indebtedness and the Noteholders be deemed to be a payment or distribution by Guarantor to or on account of Senior Indebtedness.

(b) If any payment or distribution to which the Noteholders would otherwise have been entitled but for the provisions hereof shall have been applied, pursuant to the provisions hereof, to the payment of all amounts payable under Senior Indebtedness, then and in such case, the Noteholders shall be entitled to receive from the holders of such Senior Indebtedness at the time outstanding any payments or distributions received by such holders of Senior Indebtedness in excess of the amount sufficient to pay all amounts payable under or in respect of such Senior Indebtedness in full in cash.

2.8 Guaranty Subordination Provisions Solely to Define Relative Rights. The subordination provisions hereof are and are intended solely for the purpose of defining the relative rights of the Noteholders on the one hand and the holders of Senior Indebtedness on the other hand. Nothing contained herein or in the Indenture or in the Notes is intended to or shall (a) impair, as to Guarantor, its creditors other than holders of its Senior Indebtedness and the Noteholders, the obligation of Guarantor, which is absolute and unconditional, to make payments to the Noteholders in respect of its Obligations hereof; or (b) affect the relative rights against Guarantor of the Noteholders and creditors of Guarantor other than the holders of the Senior Indebtedness; or (c) prevent the Trustee or any Noteholder from exercising all remedies otherwise permitted by applicable law upon a Default or an Event of Default under the Indenture, subject to the rights, if any, hereunder of the holders of Senior Indebtedness (1) in any case, proceeding, dissolution, liquidation or other winding-up, assignment for the benefit of creditors or other marshaling of assets and liabilities of Company referred to in Section 2.5 hereof, to receive, pursuant to and in accordance with such Section, cash, property and securities otherwise payable or deliverable to the Trustee or such Noteholder, or (2) under the conditions specified in Section 2.6 hereof, to prevent any payment prohibited by such Section or enforce their rights pursuant to Section 2.6(c) hereof.

2.9 Trustee's Relation to Senior Indebtedness. With respect to the holders of Senior Indebtedness, the Trustee undertakes to perform or to observe only such of its covenants and obligations as are specifically set forth herein, and no implied covenants or obligations with respect to the holders of Senior Indebtedness shall be read into this Guaranty against the Trustee. The Trustee shall not be deemed to owe any fiduciary duty to the holders of Senior Indebtedness and the Trustee shall not be liable to any holder of Senior Indebtedness if it shall mistakenly pay over or deliver to Noteholders, Company, Guarantor or any other Person moneys or assets to which any holder of Senior Indebtedness shall be entitled by virtue of this Guaranty or otherwise.

2.10 No Waiver of Subordination Provisions. No right of any present or future holder of any Senior Indebtedness to enforce subordination as herein provided shall at any time in any way be prejudiced or impaired by any act or failure to act on the part of Company or Guarantor or by any act or failure to act, in good faith, by any such holder, or by any non-compliance by Company or Guarantor with the terms, provisions and covenants of this Guaranty or the Indenture, regardless of any knowledge thereof any such holder may have or be otherwise charged with.



## 2.11 Notice to Trustee.

(a) Guarantor shall give prompt written notice to the Trustee of any fact known to Guarantor which would prohibit the making of any payment to or by the Trustee at its Corporate Trust Office in respect of the Notes. Notwithstanding the provisions of this Guaranty or any provision of the Indenture, the Trustee shall not be charged with knowledge of the existence of any facts which would prohibit the making of any payment to or by the Trustee in respect of the Notes, unless and until the Trustee shall have received written notice thereof from Guarantor or any Guarantor Representative or from any trustee, fiduciary or agent therefor; and, prior to the receipt of any such written notice, the Trustee, subject to the provisions of this Section 2.11, shall be entitled in all respects to assume that no such facts exist.

(b) The Trustee shall be entitled to rely on the delivery to it and Guarantor of a written notice by any Guarantor Representative to establish that such notice has been given by a holder of Senior Indebtedness (or a trustee, fiduciary or agent therefor); provided, however, that failure to give such notice to Guarantor shall not affect in any way the right of the Trustee to rely on such notice. In the event that the Trustee determines in good faith that further evidence is required with respect to the right of any Person as a holder of Senior Indebtedness to participate in any payment or distribution pursuant hereto, the Trustee may request such Person to furnish evidence to the reasonable satisfaction of the Trustee as to the amount of Senior Indebtedness held by such Person, the extent to which such Person is entitled to participate in such payment or distribution and any other facts pertinent to the rights of such Person hereunder, and if such evidence is not furnished, the Trustee may defer any payment to such Person pending judicial determination as to the right of such Person to receive such payment.

2.12 Reliance on Judicial Order or Certificate of Liquidating Agent. Upon any payment or distribution of assets of Company or Guarantor referred to herein, the Trustee, and the Noteholders shall be entitled to rely upon any order or decree entered by any court of competent jurisdiction in which such insolvency, bankruptcy, receivership, liquidation, reorganization, dissolution, winding-up or similar case or proceeding is pending, or a certificate of the trustee in bankruptcy, receiver, liquidating trustee, custodian, assignee for the benefit of creditors, agent or other Person making such payment or distribution, delivered to the Trustee or to the Noteholders, for the purpose of ascertaining the Persons entitled to participate in such payment or distribution, the holders of Senior Indebtedness and other Indebtedness of Company or Guarantor, the amount thereof or payable thereon, the amount or amounts paid or distributed thereon and all other facts pertinent thereto.

## SECTION 3

### REPRESENTATIONS AND WARRANTIES

To induce the Trustee and the Noteholders to accept this Guaranty, Guarantor hereby represents and warrants that the following statements are true and correct:

3.1 Corporate Existence. Guarantor is duly organized, validly existing and in good standing under the laws of the State of Delaware, has full corporate power and authority to own its assets and properties and to operate its business as presently owned and conducted, and as proposed to be conducted, and is qualified to do business and in good standing in every jurisdiction where its assets are located and wherever necessary to carry out its business and operations, except where failure to be so qualified or in good standing or a lack of such corporate power or authority has not had or would not have, in the aggregate, a material adverse effect.

3.2 Corporate Power; Authorization; Enforceable Obligations. Guarantor has the corporate power, authority and legal right to execute, deliver and perform this Guaranty and all obligations required hereunder and has taken all necessary corporate action to authorize its Guaranty hereunder on the terms and conditions hereof and its execution, delivery and performance of this Guaranty and all obligations required hereunder. No consent of any other Person including, without limitation, stockholders and creditors of Guarantor, and no license, permit, approval or authorization of, or exemption by, notice or report to, or registration, filing or

declaration with, any governmental authority is required by Guarantor in connection with this Guaranty or the execution, delivery, performance, validity or enforceability of this Guaranty and all obligations required hereunder, except for pursuant to the Credit Facilities. This Guaranty has been, and each instrument or document required hereunder will be, executed and delivered by a duly authorized officer of Guarantor, and this Guaranty constitutes, and each instrument or document required hereunder when executed and delivered hereunder will constitute, the legally valid and binding obligation of Guarantor, enforceable against Guarantor in accordance with its terms, except as enforcement may be limited by applicable bankruptcy, insolvency, reorganization, moratorium or other similar laws or equitable principles relating to or limiting creditors' rights generally.

3.3 No Legal Bar to this Guaranty. The execution, delivery and performance of this Guaranty and the documents or instruments required hereunder, and the use of the proceeds of the borrowings under the Indenture, will not violate any provision of any existing law or regulation binding on Guarantor, or any order, judgment, award or decree of any court, arbitrator or governmental authority binding on Guarantor, or the certificate of incorporation or bylaws of Guarantor or any securities issued by Guarantor, or any mortgage, indenture, lease, contract or other agreement, instrument or undertaking to which Guarantor is a party or by which Guarantor or any of its assets may be bound, the violation of which would have a material adverse effect on the business, operations, assets or financial condition of Guarantor and will not result in, or require, the creation or imposition of any lien on any of its property, assets or revenues pursuant to the provisions of any such mortgage, indenture, lease, contract or other agreement, instrument or undertaking.

#### SECTION 4

##### MISCELLANEOUS

4.1 Survival of Warranties. All agreements, representations and warranties made herein shall survive the execution and delivery of this Guaranty and the Indenture.

4.2 Notices. Any communications between Trustee and Guarantor and any notices or requests provided herein to be given may be given by mailing the same, postage prepaid, or by telex, facsimile transmission or cable to each such party at its address set forth below or to such other addresses as each such party may in writing hereafter indicate. Any notice, request or demand to or upon Trustee or Guarantor shall not be effective until received:

TRUSTEE:Corporate Trust Office  
1700 Market Street  
Philadelphia, PA 19103  
Attention: Corporate Trust Division  
(Renal Treatment Centers, Inc., 5 5/8%  
Convertible Subordinated Notes due 2006)

GUARANTOR:Total Renal Care Holdings, Inc.  
Suite 800  
21250 Hawthorne Boulevard  
Torrance, CA 90503  
Attention: Chief Financial Officer

4.3 Severability. In case any provision in or obligation under this Guaranty shall be invalid, illegal or unenforceable in any jurisdiction, the validity, legality and enforceability of the remaining provisions or obligations, or of such provision or obligation in any other jurisdiction, shall not in any way be affected or impaired thereby.

4.4 Amendments and Waivers. No amendment, modification, termination or waiver of any provision of this Guaranty, and no consent to any departure by Guarantor therefrom, shall in any event be effective without the written concurrence of Trustee and, in the case of any such amendment or modification, Guarantor. Any such waiver or consent shall be effective only in the specific instance and for the specific purpose for which it was given.

4.5 Headings. Section and section headings in this Guaranty are included herein for convenience of reference only and shall not constitute a part of this Guaranty for any other purpose or be given any substantive effect.

4.6 Applicable Law. THIS GUARANTY AND THE RIGHTS AND OBLIGATIONS OF GUARANTOR, TRUSTEE AND THE NOTEHOLDERS HEREUNDER SHALL BE GOVERNED BY, AND SHALL BE CONSTRUED AND ENFORCED IN ACCORDANCE WITH, THE INTERNAL LAWS OF THE STATE OF NEW YORK (INCLUDING WITHOUT LIMITATION SECTION 5-1401 OF THE GENERAL OBLIGATIONS LAW OF THE STATE OF NEW YORK), WITHOUT REGARD TO CONFLICTS OF LAWS PRINCIPLES, EXCEPT TO THE EXTENT THAT THE CODE PROVIDES THAT THE VALIDITY OR PERFECTION OF THE SECURITY INTEREST HEREUNDER, OR REMEDIES HEREUNDER, IN RESPECT OF ANY PARTICULAR COLLATERAL ARE GOVERNED BY THE LAWS OF A JURISDICTION OTHER THAN THE STATE OF NEW YORK. Unless otherwise defined herein or in the Indenture, terms used in Article 8 and Article 9 of the Uniform Commercial Code in the State of New York are used herein as therein defined.

4.7 Successors and Assigns. This Guaranty is a continuing guaranty and shall be binding upon Guarantor and its successors and assigns. This Guaranty shall inure to the benefit of Noteholders and their respective successors and assigns. Guarantor shall not assign this Guaranty or any of the rights or obligations of Guarantor hereunder without the prior written consent of Trustee. The terms and provisions of this Guaranty shall inure to the benefit of any transferee or assignee of any Note transferred or assigned in accordance with the provisions of the Indenture, and in the event of such transfer or assignment the rights and privileges herein conferred upon such Noteholder shall automatically extend to and be vested in such transferee or assignee, all subject to the terms and conditions hereof.

4.8 Consent to Jurisdiction and Service of Process. ALL JUDICIAL PROCEEDINGS BROUGHT AGAINST GUARANTOR ARISING OUT OF OR RELATING TO THIS GUARANTY, OR ANY OBLIGATIONS HEREUNDER, MAY BE BROUGHT IN ANY STATE OR FEDERAL COURT OF COMPETENT JURISDICTION IN THE STATE, COUNTY AND CITY OF NEW YORK. BY EXECUTING AND DELIVERING THIS AGREEMENT, GUARANTOR, FOR ITSELF AND IN CONNECTION WITH ITS PROPERTIES, IRREVOCABLY:

(a) ACCEPTS GENERALLY AND UNCONDITIONALLY THE NONEXCLUSIVE JURISDICTION AND VENUE OF SUCH COURTS;

(b) WAIVES ANY DEFENSE OF FORUM NON CONVENIENS;

(c) DESIGNATES AND APPOINTS CT CORPORATION SERVICES, OR SUCH OTHER PERSONS LOCATED IN NEW YORK STATE AS MAY HEREAFTER BE SELECTED BY THE GUARANTOR AND AGREEING IN WRITING TO SO SERVE, AS ITS AGENT TO RECEIVE ON ITS BEHALF SERVICE OF ALL PROCESS IN ANY SUCH PROCEEDINGS IN ANY SUCH COURT, SUCH SERVICE BEING HEREBY ACKNOWLEDGED BY THE GUARANTOR TO BE EFFECTIVE AND BINDING SERVICE IN EVERY RESPECT. A COPY OF ANY SUCH PROCESS SO SERVED SHALL BE MAILED BY REGISTERED MAIL TO THE GUARANTOR AT ITS ADDRESS PROVIDED IN ACCORDANCE WITH SECTION 4.2 PROVIDED THAT, UNLESS OTHERWISE PROVIDED BY APPLICABLE LAW, ANY FAILURE TO MAIL SUCH COPY SHALL NOT AFFECT THE VALIDITY OF SERVICE OF SUCH PROCESS. IF ANY AGENT APPOINTED BY THE GUARANTOR REFUSES TO ACCEPT SERVICE, THE

GUARANTOR HEREBY AGREES THAT SERVICE OF PROCESS SUFFICIENT FOR PERSONAL JURISDICTION IN ANY ACTION AGAINST THE GUARANTOR IN THE STATE OF NEW YORK MAY BE MADE BY REGISTERED OR CERTIFIED MAIL, RETURN RECEIPT REQUESTED, TO THE GUARANTOR AT ITS ADDRESS PROVIDED IN ACCORDANCE WITH SECTION 4.2, AND THE GUARANTOR HEREBY ACKNOWLEDGES THAT SUCH SERVICE SHALL BE EFFECTIVE AND BINDING IN EVERY RESPECT. NOTHING HEREIN SHALL AFFECT THE RIGHT TO SERVE PROCESS IN ANY OTHER MANNER PERMITTED BY LAW OR SHALL LIMIT THE RIGHT TO BRING PROCEEDINGS AGAINST THE GUARANTOR IN THE COURTS OF ANY OTHER JURISDICTION; AND

(d) AGREES THAT THE PROVISIONS OF THIS SECTION 4.8 RELATING TO JURISDICTION AND VENUE SHALL BE BINDING AND ENFORCEABLE TO THE FULLEST EXTENT PERMISSIBLE UNDER NEW YORK GENERAL OBLIGATIONS LAW SECTION 5-1402 OR OTHERWISE.

4.9 Waiver of Trial Jury. GUARANTOR AND, BY ACCEPTANCE OF THE BENEFITS HEREOF, TRUSTEE AND EACH NOTEHOLDER, EACH HEREBY AGREES TO WAIVE, TO THE EXTENT PERMITTED BY LAW, ITS RESPECTIVE RIGHTS TO A JURY TRIAL OF ANY CLAIM OR CAUSE OF ACTION BASED UPON OR ARISING OUT OF THIS GUARANTY. The scope of this waiver is intended to be all-encompassing of any and all disputes that may be filed in any court and that relate to the subject matter of this transaction, including without limitation contract claims, tort claims, breach of duty claims and all other common law and statutory claims. Guarantor and, by its acceptance of the benefits hereof, Trustee and each Noteholder each (i) acknowledges that this waiver is a material inducement for Guarantor, Trustee and each Noteholder to enter into a business relationship, that Guarantor, Trustee and each Noteholder have already relied on this waiver in entering into this Guaranty or accepting the benefits thereof, as the case may be, and that each will continue to rely on this waiver in their related future dealings with respect to the transaction contemplated hereby and (ii) further warrants and represents that each has reviewed this waiver with its legal counsel, and that each knowingly and voluntarily waives its jury trial rights following consultation with legal counsel. THIS WAIVER IS IRREVOCABLE, MEANING THAT IT MAY NOT BE MODIFIED EITHER ORALLY OR IN WRITING (OTHER THAN BY A MUTUAL WRITTEN WAIVER SPECIFICALLY REFERRING TO THIS SECTION 4.9 AND EXECUTED BY GUARANTIED PARTY AND GUARANTOR), AND THIS WAIVER SHALL APPLY TO ANY SUBSEQUENT AMENDMENTS, RENEWALS, SUPPLEMENTS OR MODIFICATIONS TO THIS GUARANTY. In the event of litigation, this Guaranty may be filed as a written consent to a trial by the court.

4.10 No Other Writing. This writing is intended by Guarantor, Trustee and each Noteholder as the final expression of this Guaranty and is also intended as a complete and exclusive statement of the terms of their agreement with respect to the matters covered hereby. No course of dealing, course of performance or trade usage, and no parol evidence of any nature, shall be used to supplement or modify any terms of this Guaranty. There are no conditions to the full effectiveness of this Guaranty.

4.11 Further Assurances. At any time or from time to time, upon the request of Trustee, Guarantor shall execute and deliver such further documents and do such other acts and things as Trustee may reasonably request in order to effect fully the purposes of this Guaranty.

4.12 Trustee as Agent.

(a) Trustee has been appointed to act as Trustee hereunder by the Noteholders. Trustee shall be obligated, and shall have the right hereunder, to make demands, to give notices, to exercise or refrain from exercising any rights, and to take or refrain from taking any action, solely in accordance with this Guaranty and the Indenture.

(b) Trustee shall at all times be the same Person that is Trustee under the Indenture. Written notice of resignation by Trustee pursuant to Section 8.10 of the Indenture shall also constitute notice of resignation as

Trustee under this Guaranty; removal of Trustee pursuant to Section 8.10 of the Indenture shall also constitute removal as Trustee under this Guaranty; and appointment of a successor Trustee pursuant to Section 8.10 of the Indenture shall also constitute appointment of a successor Trustee under this Guaranty. Upon the acceptance of any appointment as Trustee under Section 8.10 of the Indenture by a successor Trustee, that successor Trustee shall thereupon succeed to and become vested with all the rights, powers, privileges and duties of the retiring or removed Trustee under this Guaranty, and the retiring or removed Trustee under this Guaranty shall promptly (i) transfer to such successor Trustee all sums held hereunder, together with all records and other documents necessary or appropriate in connection with the performance of the duties of the successor Trustee under this Guaranty, and (ii) take such other actions as may be necessary or appropriate in connection with the assignment to such successor Trustee of the rights created hereunder, whereupon such retiring or removed Trustee shall be discharged from its duties and obligations under this Guaranty. After any retiring or removed Trustee's resignation or removal hereunder as Trustee, the provisions of this Guaranty shall inure to its benefit as to any actions taken or omitted to be taken by it under this Guaranty while it was Trustee hereunder.

IN WITNESS WHEREOF, Guarantor has caused this Guaranty to be duly executed and delivered by its officer thereunto duly authorized as of the date first written above.

TOTAL RENAL CARE HOLDINGS, INC.

By: \_\_\_\_\_  
Name:  
Title:

## GUARANTY

This Guaranty (this "Guaranty") is entered into as of March 31, 1998 by Total Renal Care Holdings, Inc., a Delaware corporation ("Guarantor"), in favor of PNC Bank, National Association, as Trustee ("Trustee"), for the benefit of the noteholders ("Noteholders") under that certain Indenture, dated as of June 12, 1996, between Renal Treatment Centers, Inc., a Delaware corporation and wholly owned subsidiary of Guarantor ("Company"), and Trustee, as amended by that certain First Supplemental Indenture, dated as of February 27, 1998, between Company, Guarantor and Trustee (as amended, supplemented or otherwise modified from time to time, the "Indenture") with respect to Company's 5 5/8% Convertible Subordinated Notes due 2006 (the "Notes"). Unless otherwise defined herein, capitalized terms used in this Guaranty shall have the meanings assigned to such terms in the Indenture.

## RECITALS

A. Company became a wholly owned subsidiary of Guarantor pursuant to that certain Agreement and Plan of Merger by and among Guarantor, Nevada Acquisition Corp., a Delaware corporation, and Company, dated as of November 18, 1997 (the "Merger").

B. Guarantor has determined that it is in its best interest irrevocably and unconditionally to guaranty the Notes.

Now, therefore, based upon the foregoing and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Guarantor hereby agrees as follows:

## SECTION 1

## DEFINITIONS

1.1 Certain Defined Terms. As used in this Guaranty, the following terms shall have the following meanings unless the context otherwise requires:

"Additional Interest" means additional interest on the Notes pursuant to Section 2.3 of the Indenture which Company and Guarantor, jointly and severally, hereby agree to pay to the Noteholders

"Credit Facilities" means, collectively, (i) Guarantor's \$800,000,000 Revolving Credit Agreement, dated as of October 24, 1997 with DLJ Capital Funding, Inc., as Syndication Agent, First Union National Bank, as Documentation Agent, The Bank of New York, as Administrative Agent, BNY Capital Markets, Inc. and Donaldson, Lufkin & Jenrette Securities Corporation, as Co-Arrangers, and the various lenders party thereto, together with the promissory notes issued thereunder and the other documents related thereto, and (ii) Guarantor's \$250,000,000 Term Loan Agreement, dated as of October 24, 1997, with DLJ Capital Funding, Inc., as Syndication Agent, The Bank of New York, as Administrative Agent, BNY Capital Markets, Inc. and Donaldson, Lufkin & Jenrette Securities Corporation, as Co-Arrangers, and the various lenders party thereto, together with the promissory notes issued thereunder and the other documents related thereto, in each case as such agreements may be amended (including any amendment and restatement thereof), supplemented or otherwise modified from time to time, including any agreements extending the maturity of, refinancing, replacing or otherwise restructuring (including increasing the amount of available borrowings thereunder or adding subsidiaries of Guarantor and/or Company as additional borrowers or guarantors thereunder) all or any portion of the Indebtedness and other Obligations under such agreements and whether by the same or any other agent, lender or group of lenders.

"Designated Senior Indebtedness" means any Indebtedness under either of the Credit Facilities and any other Indebtedness in an original principal amount of at least \$50 million, provided that by its terms such Indebtedness expressly provides that it is "Designated Senior Indebtedness" for purposes of this Guaranty.

"Indebtedness" means (without duplication), with respect to any Person, any obligation at any time outstanding, secured or unsecured, contingent or otherwise, which is for borrowed money (whether or not the recourse of the lender is to the whole of the assets of such Person or only to a portion thereof), or evidenced by bonds, notes, debentures or similar instruments or representing the balance deferred and unpaid of the purchase price of any property (excluding, without limitation, any balance that constitutes accounts payable or trade payables, and other accrued liabilities arising in the ordinary course of business) if and to the extent any of the foregoing indebtedness would appear as a liability upon a balance sheet of such Person prepared in accordance with generally accepted accounting principles ("GAAP"), and shall also include, to the extent not otherwise included, (i) any obligations secured by a lien to which the property or assets owned or held by such Person is subject, whether or not the obligation or obligations secured thereby shall have been assumed, to the extent of the fair market value of such property or assets, (ii) guarantees of items of other Persons which would be included within this definition for such other Persons (whether or not such items would appear upon the balance sheet of the guarantor), to the extent of the amount of the Indebtedness so guaranteed, and (iii) all obligations for the reimbursement of any obligor on any letter of credit, banker's acceptance or similar credit transaction. The amount of Indebtedness of any Person at any date shall be the outstanding balance at such date of all unconditional obligations as described above and, with respect to contingent obligations, the maximum liability upon the occurrence of the contingency giving rise to the obligations; provided, that (i) the amount outstanding at any time of any Indebtedness issued with original issue discount is the principal amount of such Indebtedness less the remaining unamortized portion of the original issue discount of such Indebtedness at such time as determined in conformity with GAAP and (ii) Indebtedness shall not include any liability for federal, state, local or other taxes. Notwithstanding any other provision of the foregoing definition, any trade payable arising from the purchase of goods or materials or for the services obtained in the ordinary course of business shall not be deemed to be "Indebtedness." Furthermore, guarantees of (or obligations with respect to letters of credit supporting) Indebtedness otherwise included in the determination of such amount shall not also be included.

"Non-Payment Event of Default" means any event (other than a Payment Default) the occurrence of which entitles one or more Persons to accelerate the maturity of any Designated Senior Indebtedness.

"Obligations" means, with respect to any Indebtedness, any principal, premium, interest, penalties, fees, indemnifications, reimbursements, damages and other expenses payable under the documentation governing such Indebtedness.

"Payment Default" means any default, whether or not any requirement for the giving of notice, the lapse of time or both, or any other condition to such default becoming an event of default has occurred, in the payment of principal of or premium, if any, or interest on or any other amount payable in connection with any Designated Senior Indebtedness.

"Person" means any individual, corporation, company (including any limited liability company), partnership, joint venture, trust, unincorporated organization, government or any agency or political subdivision thereof or any other entity.

"Senior Indebtedness," as to Guarantor, means the principal of and premium, if any, and interest on, and any and all other fees, expense reimbursement obligations and all other Obligations and amounts due pursuant to the terms of all agreements, documents and instruments providing for, creating, securing or evidencing or otherwise entered into in connection with (a) all Indebtedness of Guarantor owed to lenders or agents under either of the Credit Facilities, (b) all obligations of Guarantor to reimburse any bank or other person in respect of amounts paid under letters of credit, acceptances or other similar instruments and all obligations of Guarantor with respect to guarantees of such reimbursement obligations, (c) all other Indebtedness of Guarantor which does not provide that it is to be ranked *pari passu* with or subordinate to the Guaranty and (d) all deferrals, renewals,

refinancings, extensions and refundings of, and amendments, modifications and supplements to, any of the Senior Indebtedness described above. Notwithstanding anything to the contrary in the foregoing, Senior Indebtedness will not include (i) Indebtedness of Guarantor to any of its Subsidiaries, or to any Affiliate of Guarantor or any of such Affiliate's Subsidiaries, (ii) Indebtedness represented by the Guaranty, (iii) any Indebtedness which by the express terms of the agreement or instrument creating, evidencing or governing the same is junior or subordinate in right of payment to any item of Senior Indebtedness, (iv) any trade payable arising from the purchase of goods or materials or for services obtained in the ordinary course of business, and (v) any Indebtedness to or guaranteed on behalf of, any stockholders, director, officer or employee of Guarantor or any Subsidiary of Guarantor.

## SECTION 2

### THE GUARANTY

#### 2.1 Guaranty.

(a) Subject to the provisions hereof, Guarantor hereby unconditionally guarantees in favor of the Trustee for the benefit of the Noteholders, (i) the due and punctual payment of the principal of, and premium, if any, and interest on each Note, when and as the same shall become due and payable, subject to any applicable grace period, whether at maturity, by acceleration or otherwise, the due and punctual payment of interest on the overdue principal of, and premium, if any, and interest on the Notes, to the extent lawful, and the due and punctual performance of all other Obligations of Company to the Noteholders or the Trustee all in accordance with the terms of such Note and the Indenture, subject, however, to the limitations set forth in Section 2.2, and (ii) in the case of any extension of time of payment or renewal of any Notes or any of such other Obligations, that the same will be promptly paid in full when due or performed in accordance with the terms of the extension or renewal, at stated maturity, by acceleration or otherwise. Guarantor hereby agrees that its obligations thereunder and hereunder shall be absolute and unconditional, irrespective of, and shall be unaffected by, any invalidity, irregularity or unenforceability of any such Note or the Indenture, any failure to enforce the provisions of any such Note or the Indenture, any waiver, modification or indulgence granted to Company with respect thereto by the Noteholder of such Note or the Trustee, or any other circumstances which may otherwise constitute a legal or equitable discharge of a surety or Guarantor.

(b) Guarantor hereby waives diligence, presentment, demand for payment, filing of claims with a court in the event of merger or bankruptcy of Company, any right to require a proceeding first against Company, protest or notice with respect to any such Note or the Indebtedness evidenced thereby and all demands whatsoever, and covenants that this Guaranty will not be discharged as to any such Note except by payment in full of the principal thereof, premium if any, and interest thereon and as provided in Section 13.1 of the Indenture. Guarantor further agrees that, as between Guarantor, on the one hand, and the Noteholders and the Trustee, on the other hand, (i) the maturity of the Obligations guaranteed hereby may be accelerated as provided in Article 7 of the Indenture for the purposes of this Guaranty, notwithstanding any stay, injunction or other prohibition preventing such acceleration in respect of the Obligations guaranteed hereby, and (ii) in the event of any declaration of acceleration of such Obligations as provided in Article 7 of the Indenture, such Obligations (whether or not due and payable) shall forthwith become due and payable by Guarantor for the purpose of this Guaranty. In addition, without limiting the foregoing provisions, upon the effectiveness of an acceleration under Article 7 of the Indenture, the Trustee shall promptly make a demand for payment on the Notes under the Guaranty provided for herein and not discharged.

2.2 Effectiveness of Guaranty. Guarantor agrees that this Guaranty shall be and remain in full force and effect notwithstanding any failure to endorse on each Note a notation of such Guaranty and that each Note shall be entitled to the full benefit of the Guaranty whether or not the Guaranty is notated thereon.

2.3 Limitation of Guaranty. Notwithstanding any term or provision of the Indenture to the contrary, the maximum aggregate amount of the obligations guaranteed hereunder by Guarantor shall not exceed the maximum amount that can be guaranteed hereunder by Guarantor without rendering the Guaranty, as it relates to



Guarantor, voidable under applicable law relating to fraudulent conveyance or fraudulent transfer or similar laws affecting the rights of creditors generally.

#### 2.4 Guaranty Obligations Subordinated to Guarantor Senior Indebtedness.

(a) Guarantor hereby covenants and agrees that, to the extent and in the manner set forth herein, the Indebtedness represented by the Guaranty and the payment of the principal of, premium, if any, and interest on the Notes pursuant to the Guaranty by Guarantor are hereby expressly made subordinate and subject in right of payment as provided herein to the prior indefeasible payment and satisfaction in full in cash of all Senior Indebtedness.

(b) The holders of Senior Indebtedness (including, without limitation, Designated Senior Indebtedness) shall have the right to rely on this Section 2.4 and the following Section 2.5 through Section 2.12, and such provisions are made for the benefit of the holders of Senior Indebtedness; and such holders are made obligees hereunder and they or each of them may enforce such provisions, and no amendment or modification of the provisions contained herein shall diminish the rights of such holders unless such holders have agreed in writing thereto.

2.5 Payment Over of Proceeds upon Dissolution, etc., of Guarantor. In the event of (x) any insolvency or bankruptcy case or proceeding, or any receivership, arrangement, reorganization, liquidation, dissolution or other similar case or proceeding in connection therewith whether or not involving insolvency or bankruptcy, relative to Guarantor or to its creditors, as such, or to its assets, whether voluntary or involuntary, or (y) any general assignment for the benefit of creditors or other marshaling of assets or liabilities of Guarantor (except in connection with the merger or consolidation of Guarantor or its liquidation or dissolution following the transfer of all or substantially all of its assets, upon the terms and conditions that would be permitted under Article 12 of the Indenture if references to "Company" were to Guarantor) (all of the foregoing referred to herein individually as a "Guarantor Bankruptcy Proceeding" and collectively as "Guarantor Bankruptcy Proceedings"), then and in any such event:

i. the holders of all Senior Indebtedness shall be entitled to receive payment and satisfaction in full in cash of all amounts due on or in respect of all such Senior Indebtedness (including any interest accruing after the commencement of any such Guarantor Bankruptcy Proceeding whether or not such interest is an allowable claim enforceable against Company in any such proceeding) before the Noteholders are entitled to receive or retain, pursuant to this Guaranty, any payment or distribution of any kind by Guarantor on account of this Guaranty;

ii. any payment or distribution of assets of Guarantor of any kind or character, whether in cash, property or securities, by set-off or otherwise, to which the Noteholders or the Trustee would be entitled but for the subordination provisions hereof shall be paid by the liquidating trustee or agent or other Person making such payment or distribution, whether a trustee in bankruptcy, a receiver or liquidating trustee or otherwise, directly to the holders of Senior Indebtedness or their representative or representatives or to the trustee or trustees under any indenture under which any instruments evidencing any of such Senior Indebtedness may have been issued, ratably according to the aggregate amounts remaining unpaid on account of such Senior Indebtedness held or represented by each, to the extent necessary to make payment in full in cash of all such Senior Indebtedness remaining unpaid, after giving effect to any concurrent payment or distribution, or provision therefor, to the holders of such Senior Indebtedness;

iii. in the event that, notwithstanding the foregoing provisions of this Section 2.5, the Trustee or the Noteholder of any Note shall have received any payment or distribution of assets of Guarantor of any kind or character, whether in cash, property or securities, including, without limitation, by way of set-off or otherwise, in respect of this Guaranty before all Senior Indebtedness is paid and satisfied in full in cash, then such payment or distribution shall be held by the recipient in trust for the benefit of holders of such Senior Indebtedness and shall be immediately paid over or delivered to the holders of such Senior Indebtedness or their representative or representatives to the extent necessary to make payment in full in cash of all such Senior Indebtedness remaining unpaid after giving effect to any concurrent payment or distribution to or for the holders of such Senior Indebtedness; and

iv. the consolidation of Guarantor with, or the merger of Guarantor with or into, another Person or the liquidation or dissolution of Guarantor following the conveyance, transfer or lease of its properties and assets substantially as an entirety to another Person upon the terms and conditions set forth herein shall not be deemed a dissolution, winding-up, liquidation, reorganization, assignment for the benefit of creditors or marshaling of assets and liabilities of such Guarantor for, as would be applicable as if references to "Company" were to Guarantor, the purposes of Article 12 of the Indenture if the Person formed by such consolidation or the surviving entity of such merger or the Person which acquires by conveyance, transfer or lease such properties and assets substantially as an entirety, as the case may be, shall, as a part of such consolidation, merger, conveyance, transfer or lease, comply with the conditions set forth in such Article 12 of the Indenture, as would be applicable as if references to "Company" were to Guarantor.

## 2.6 Suspension of Guaranty Obligations When Senior Indebtedness in Default.

(a) Unless Section 2.5 hereof shall be applicable, after the occurrence of a Payment Default with respect to any Designated Senior Indebtedness which constitutes Senior Indebtedness, no payment or distribution of any kind or character of Guarantor (including, without limitation, cash, property and any payment or distribution which may be payable or deliverable by reason of the payment of any other Indebtedness of Guarantor being subordinated to its Obligations herein) may be made by or on behalf of Guarantor, including, without limitation, by way of set-off or otherwise, for or on account hereof, and neither the Trustee nor any Noteholder shall take or receive from Guarantor, directly or indirectly in any manner, payment in respect of all or any portion of its Obligations hereof commencing on the date of receipt by the Trustee of written notice from any representative of the holders of any Designated Senior Indebtedness which constitutes Senior Indebtedness (each, a "Guarantor Representative") of such Payment Default, and in any such event, such prohibition shall continue until such Payment Default is cured, waived in writing or ceases to exist. At such time as the prohibition set forth in the preceding sentence shall no longer be in effect, subject to the provisions of the preceding and following paragraph, Guarantor shall resume making any and all required payments in respect hereof, including any missed payments.

(b) Unless Section 2.5 hereof shall be applicable, upon the occurrence of a Non-Payment Event of Default on Designated Senior Indebtedness, no payment or distribution of any kind or character (including, without limitation, cash, property and any payment or distribution which may be payable or deliverable by reason of the payment of any other Indebtedness of Guarantor being subordinated to its Obligations herein) shall be made by Guarantor, including, without limitation, by way of set-off or otherwise, for or on account of any of its Obligations herein, and neither the Trustee nor any Noteholder shall take or receive from Guarantor, directly or indirectly in any manner, payment in respect of all or any portion of its obligations on its Guaranty for a period (a "Guaranty Payment Blockage Period") commencing on the date of receipt by the Trustee of written notice from any Guarantor Representative of such Non-Payment Event of Default, unless and until (subject to any blockage of payments that may then be in effect under the preceding paragraphs), the earlier of: (x) the date that such Non-Payment Event of Default shall have been cured or waived in writing or shall have ceased to exist or such Designated Senior Indebtedness shall have been paid in full in cash or (y) the date that such Guaranty Payment Blockage Period shall have been terminated by written notice to Guarantor or the Trustee from the applicable Guarantor Representative, after which, in the case of clause (x) or (y), Guarantor shall resume making any and all required payments in respect of its Obligations herein, including any missed payments. Any number of additional Guaranty Payment Blockage Periods may be commenced during any Guaranty Payment Blockage Period.

(c) In the event that, notwithstanding the foregoing, the Trustee or any Noteholder shall have received any payment or distribution from Guarantor prohibited by the foregoing provisions of this Section 2.6, then and in such event such payment or distribution shall be held in trust for the benefit of and shall be paid over and delivered forthwith to the holders of the Senior Indebtedness or their representative or representatives for distribution to the holders of Senior Indebtedness or, if no amounts are then due in respect of Senior Indebtedness, promptly returned to Guarantor, or otherwise as a court of competent jurisdiction shall direct.

## 2.7 Subrogation to Rights of Noteholders of Senior Indebtedness.

(a) Upon the payment in full in cash of all Senior Indebtedness, the Noteholders shall be subrogated to the rights of the holders of such Senior Indebtedness to receive payments and distributions of cash, property and securities of Guarantor made on such Senior Indebtedness until all amounts due to be paid hereunder shall be paid in full. For purposes of such subrogation, no payments or distributions to holders of Senior Indebtedness of any cash, property or securities to which Noteholders or the Trustee would be entitled except for the provisions hereof, and no payments over pursuant to the provisions hereof to holders of Senior Indebtedness by Noteholders or the Trustee, shall, as among Guarantor, its creditors other than holders of Senior Indebtedness and the Noteholders be deemed to be a payment or distribution by Guarantor to or on account of Senior Indebtedness.

(b) If any payment or distribution to which the Noteholders would otherwise have been entitled but for the provisions hereof shall have been applied, pursuant to the provisions hereof, to the payment of all amounts payable under Senior Indebtedness, then and in such case, the Noteholders shall be entitled to receive from the holders of such Senior Indebtedness at the time outstanding any payments or distributions received by such holders of Senior Indebtedness in excess of the amount sufficient to pay all amounts payable under or in respect of such Senior Indebtedness in full in cash.

2.8 Guaranty Subordination Provisions Solely to Define Relative Rights. The subordination provisions hereof are and are intended solely for the purpose of defining the relative rights of the Noteholders on the one hand and the holders of Senior Indebtedness on the other hand. Nothing contained herein or in the Indenture or in the Notes is intended to or shall (a) impair, as to Guarantor, its creditors other than holders of its Senior Indebtedness and the Noteholders, the obligation of Guarantor, which is absolute and unconditional, to make payments to the Noteholders in respect of its Obligations hereof; or (b) affect the relative rights against Guarantor of the Noteholders and creditors of Guarantor other than the holders of the Senior Indebtedness; or (c) prevent the Trustee or any Noteholder from exercising all remedies otherwise permitted by applicable law upon a Default or an Event of Default under the Indenture, subject to the rights, if any, hereunder of the holders of Senior Indebtedness (1) in any case, proceeding, dissolution, liquidation or other winding-up, assignment for the benefit of creditors or other marshaling of assets and liabilities of Company referred to in Section 2.5 hereof, to receive, pursuant to and in accordance with such Section, cash, property and securities otherwise payable or deliverable to the Trustee or such Noteholder, or (2) under the conditions specified in Section 2.6 hereof, to prevent any payment prohibited by such Section or enforce their rights pursuant to Section 2.6(c) hereof.

2.9 Trustee's Relation to Senior Indebtedness. With respect to the holders of Senior Indebtedness, the Trustee undertakes to perform or to observe only such of its covenants and obligations as are specifically set forth herein, and no implied covenants or obligations with respect to the holders of Senior Indebtedness shall be read into this Guaranty against the Trustee. The Trustee shall not be deemed to owe any fiduciary duty to the holders of Senior Indebtedness and the Trustee shall not be liable to any holder of Senior Indebtedness if it shall mistakenly pay over or deliver to Noteholders, Company, Guarantor or any other Person moneys or assets to which any holder of Senior Indebtedness shall be entitled by virtue of this Guaranty or otherwise.

2.10 No Waiver of Subordination Provisions. No right of any present or future holder of any Senior Indebtedness to enforce subordination as herein provided shall at any time in any way be prejudiced or impaired by any act or failure to act on the part of Company or Guarantor or by any act or failure to act, in good faith, by any such holder, or by any non-compliance by Company or Guarantor with the terms, provisions and covenants of this Guaranty or the Indenture, regardless of any knowledge thereof any such holder may have or be otherwise charged with.

## 2.11 Notice to Trustee.

(a) Guarantor shall give prompt written notice to the Trustee of any fact known to Guarantor which would prohibit the making of any payment to or by the Trustee at its Corporate Trust Office in respect of the Notes. Notwithstanding the provisions of this Guaranty or any provision of the Indenture, the Trustee shall not be charged with knowledge of the existence of any facts which would prohibit the making of any payment to or by

the Trustee in respect of the Notes, unless and until the Trustee shall have received written notice thereof from Guarantor or any Guarantor Representative or from any trustee, fiduciary or agent therefor; and, prior to the receipt of any such written notice, the Trustee, subject to the provisions of this Section 2.11, shall be entitled in all respects to assume that no such facts exist.

(b) The Trustee shall be entitled to rely on the delivery to it and Guarantor of a written notice by any Guarantor Representative to establish that such notice has been given by a holder of Senior Indebtedness (or a trustee, fiduciary or agent therefor); provided, however, that failure to give such notice to Guarantor shall not affect in any way the right of the Trustee to rely on such notice. In the event that the Trustee determines in good faith that further evidence is required with respect to the right of any Person as a holder of Senior Indebtedness to participate in any payment or distribution pursuant hereto, the Trustee may request such Person to furnish evidence to the reasonable satisfaction of the Trustee as to the amount of Senior Indebtedness held by such Person, the extent to which such Person is entitled to participate in such payment or distribution and any other facts pertinent to the rights of such Person hereunder, and if such evidence is not furnished, the Trustee may defer any payment to such Person pending judicial determination as to the right of such Person to receive such payment.

2.12 Reliance on Judicial Order or Certificate of Liquidating Agent. Upon any payment or distribution of assets of Company or Guarantor referred to herein, the Trustee, and the Noteholders shall be entitled to rely upon any order or decree entered by any court of competent jurisdiction in which such insolvency, bankruptcy, receivership, liquidation, reorganization, dissolution, winding-up or similar case or proceeding is pending, or a certificate of the trustee in bankruptcy, receiver, liquidating trustee, custodian, assignee for the benefit of creditors, agent or other Person making such payment or distribution, delivered to the Trustee or to the Noteholders, for the purpose of ascertaining the Persons entitled to participate in such payment or distribution, the holders of Senior Indebtedness and other Indebtedness of Company or Guarantor, the amount thereof or payable thereon, the amount or amounts paid or distributed thereon and all other facts pertinent thereto.

### SECTION 3

#### REPRESENTATIONS AND WARRANTIES

To induce the Trustee and the Noteholders to accept this Guaranty, Guarantor hereby represents and warrants that the following statements are true and correct:

3.1 Corporate Existence. Guarantor is duly organized, validly existing and in good standing under the laws of the State of Delaware, has full corporate power and authority to own its assets and properties and to operate its business as presently owned and conducted, and as proposed to be conducted, and is qualified to do business and in good standing in every jurisdiction where its assets are located and wherever necessary to carry out its business and operations, except where failure to be so qualified or in good standing or a lack of such corporate power or authority has not had or would not have, in the aggregate, a material adverse effect.

3.2 Corporate Power; Authorization; Enforceable Obligations. Guarantor has the corporate power, authority and legal right to execute, deliver and perform this Guaranty and all obligations required hereunder and has taken all necessary corporate action to authorize its Guaranty hereunder on the terms and conditions hereof and its execution, delivery and performance of this Guaranty and all obligations required hereunder. No consent of any other Person including, without limitation, stockholders and creditors of Guarantor, and no license, permit, approval or authorization of, or exemption by, notice or report to, or registration, filing or declaration with, any governmental authority is required by Guarantor in connection with this Guaranty or the execution, delivery, performance, validity or enforceability of this Guaranty and all obligations required hereunder, except for pursuant to the Credit Facilities. This Guaranty has been, and each instrument or document required hereunder will be, executed and delivered by a duly authorized officer of Guarantor, and this Guaranty constitutes, and each instrument or document required hereunder when executed and delivered hereunder will constitute, the legally valid and binding obligation of Guarantor, enforceable against Guarantor in accordance

with its terms, except as enforcement may be limited by applicable bankruptcy, insolvency, reorganization, moratorium or other similar laws or equitable principles relating to or limiting creditors' rights generally.

3.3 No Legal Bar to this Guaranty. The execution, delivery and performance of this Guaranty and the documents or instruments required hereunder, and the use of the proceeds of the borrowings under the Indenture, will not violate any provision of any existing law or regulation binding on Guarantor, or any order, judgment, award or decree of any court, arbitrator or governmental authority binding on Guarantor, or the certificate of incorporation or bylaws of Guarantor or any securities issued by Guarantor, or any mortgage, indenture, lease, contract or other agreement, instrument or undertaking to which Guarantor is a party or by which Guarantor or any of its assets may be bound, the violation of which would have a material adverse effect on the business, operations, assets or financial condition of Guarantor and will not result in, or require, the creation or imposition of any lien on any of its property, assets or revenues pursuant to the provisions of any such mortgage, indenture, lease, contract or other agreement, instrument or undertaking.

#### SECTION 4

##### MISCELLANEOUS

4.1 Survival of Warranties. All agreements, representations and warranties made herein shall survive the execution and delivery of this Guaranty and the Indenture.

4.2 Notices. Any communications between Trustee and Guarantor and any notices or requests provided herein to be given may be given by mailing the same, postage prepaid, or by telex, facsimile transmission or cable to each such party at its address set forth below or to such other addresses as each such party may in writing hereafter indicate. Any notice, request or demand to or upon Trustee or Guarantor shall not be effective until received:

TRUSTEE: Corporate Trust Office  
1700 Market Street  
Philadelphia, PA 19103  
Attention:  
Corporate Trust Division  
(Renal Treatment Centers, Inc., 5 5/8%  
Convertible Subordinated Notes due 2006)

GUARANTOR: Total Renal Care Holdings, Inc.  
Suite 800  
21250 Hawthorne Boulevard  
Torrance, CA 90503  
Attention: Chief Financial Officer

4.3 Severability. In case any provision in or obligation under this Guaranty shall be invalid, illegal or unenforceable in any jurisdiction, the validity, legality and enforceability of the remaining provisions or obligations, or of such provision or obligation in any other jurisdiction, shall not in any way be affected or impaired thereby.

4.4 Amendments and Waivers. No amendment, modification, termination or waiver of any provision of this Guaranty, and no consent to any departure by Guarantor therefrom, shall in any event be effective without the written concurrence of Trustee and, in the case of any such amendment or modification, Guarantor. Any such waiver or consent shall be effective only in the specific instance and for the specific purpose for which it was given.

4.5 Headings. Section and section headings in this Guaranty are included herein for convenience of reference only and shall not constitute a part of this Guaranty for any other purpose or be given any substantive effect.

4.6 Applicable Law. THIS GUARANTY AND THE RIGHTS AND OBLIGATIONS OF GUARANTOR, TRUSTEE AND THE NOTEHOLDERS HEREUNDER SHALL BE GOVERNED BY, AND SHALL BE CONSTRUED AND ENFORCED IN ACCORDANCE WITH, THE INTERNAL LAWS OF THE STATE OF NEW YORK (INCLUDING WITHOUT LIMITATION SECTION 5-1401 OF THE GENERAL OBLIGATIONS LAW OF THE STATE OF NEW YORK), WITHOUT REGARD TO CONFLICTS OF LAWS PRINCIPLES, EXCEPT TO THE EXTENT THAT THE CODE PROVIDES THAT THE VALIDITY OR PERFECTION OF THE SECURITY INTEREST HEREUNDER, OR REMEDIES HEREUNDER, IN RESPECT OF ANY PARTICULAR COLLATERAL ARE GOVERNED BY THE LAWS OF A JURISDICTION OTHER THAN THE STATE OF NEW YORK. Unless otherwise defined herein or in the Indenture, terms used in Article 8 and Article 9 of the Uniform Commercial Code in the State of New York are used herein as therein defined.

4.7 Successors and Assigns. This Guaranty is a continuing guaranty and shall be binding upon Guarantor and its successors and assigns. This Guaranty shall inure to the benefit of Noteholders and their respective successors and assigns. Guarantor shall not assign this Guaranty or any of the rights or obligations of Guarantor hereunder without the prior written consent of Trustee. The terms and provisions of this Guaranty shall inure to the benefit of any transferee or assignee of any Note transferred or assigned in accordance with the provisions of the Indenture, and in the event of such transfer or assignment the rights and privileges herein conferred upon such Noteholder shall automatically extend to and be vested in such transferee or assignee, all subject to the terms and conditions hereof.

4.8 Consent to Jurisdiction and Service of Process. ALL JUDICIAL PROCEEDINGS BROUGHT AGAINST GUARANTOR ARISING OUT OF OR RELATING TO THIS GUARANTY, OR ANY OBLIGATIONS HEREUNDER, MAY BE BROUGHT IN ANY STATE OR FEDERAL COURT OF COMPETENT JURISDICTION IN THE STATE, COUNTY AND CITY OF NEW YORK. BY EXECUTING AND DELIVERING THIS AGREEMENT, GUARANTOR, FOR ITSELF AND IN CONNECTION WITH ITS PROPERTIES, IRREVOCABLY:

(A) ACCEPTS GENERALLY AND UNCONDITIONALLY THE NONEXCLUSIVE JURISDICTION AND VENUE OF SUCH COURTS;

(B) WAIVES ANY DEFENSE OF FORUM NON CONVENIENS;

(C) DESIGNATES AND APPOINTS CT CORPORATION SERVICES, OR SUCH OTHER PERSONS LOCATED IN NEW YORK STATE AS MAY HEREAFTER BE SELECTED BY THE GUARANTOR AND AGREEING IN WRITING TO SO SERVE, AS ITS AGENT TO RECEIVE ON ITS BEHALF SERVICE OF ALL PROCESS IN ANY SUCH PROCEEDINGS IN ANY SUCH COURT, SUCH SERVICE BEING HEREBY ACKNOWLEDGED BY THE GUARANTOR TO BE EFFECTIVE AND BINDING SERVICE IN EVERY RESPECT. A COPY OF ANY SUCH PROCESS SO SERVED SHALL BE MAILED BY REGISTERED MAIL TO THE GUARANTOR AT ITS ADDRESS PROVIDED IN ACCORDANCE WITH SECTION 4.2 PROVIDED THAT, UNLESS OTHERWISE PROVIDED BY APPLICABLE LAW, ANY FAILURE TO MAIL SUCH COPY SHALL NOT AFFECT THE VALIDITY OF SERVICE OF SUCH PROCESS. IF ANY AGENT APPOINTED BY THE GUARANTOR REFUSES TO ACCEPT SERVICE, THE GUARANTOR HEREBY AGREES THAT SERVICE OF PROCESS SUFFICIENT FOR PERSONAL JURISDICTION IN ANY ACTION AGAINST THE GUARANTOR IN THE STATE OF NEW YORK MAY BE MADE BY REGISTERED OR CERTIFIED MAIL, RETURN RECEIPT REQUESTED, TO THE GUARANTOR AT ITS ADDRESS PROVIDED IN ACCORDANCE WITH SECTION 4.2, AND THE GUARANTOR HEREBY ACKNOWLEDGES THAT SUCH SERVICE SHALL BE EFFECTIVE AND BINDING IN EVERY RESPECT. NOTHING HEREIN SHALL AFFECT THE RIGHT TO SERVE PROCESS IN ANY OTHER MANNER PERMITTED BY LAW OR SHALL LIMIT THE RIGHT TO BRING PROCEEDINGS AGAINST THE GUARANTOR IN THE COURTS OF ANY OTHER JURISDICTION; AND

(D) AGREES THAT THE PROVISIONS OF THIS SECTION 4.8 RELATING TO JURISDICTION AND VENUE SHALL BE BINDING AND ENFORCEABLE TO THE FULLEST EXTENT PERMISSIBLE UNDER NEW YORK GENERAL OBLIGATIONS LAW SECTION 5-1402 OR OTHERWISE.

4.9 Waiver of Trial Jury. GUARANTOR AND, BY ACCEPTANCE OF THE BENEFITS HEREOF, TRUSTEE AND EACH NOTEHOLDER, EACH HEREBY AGREES TO WAIVE, TO THE EXTENT PERMITTED BY LAW, ITS RESPECTIVE RIGHTS TO A JURY TRIAL OF ANY CLAIM OR CAUSE OF ACTION BASED UPON OR ARISING OUT OF THIS GUARANTY. The scope of this waiver is intended to be all-encompassing of any and all disputes that may be filed in any court and that relate to the subject matter of this transaction, including without limitation contract claims, tort claims, breach of duty claims and all other common law and statutory claims. Guarantor and, by its acceptance of the benefits hereof, Trustee and each Noteholder each (i) acknowledges that this waiver is a material inducement for Guarantor, Trustee and each Noteholder to enter into a business relationship, that Guarantor, Trustee and each Noteholder have already relied on this waiver in entering into this Guaranty or accepting the benefits thereof, as the case may be, and that each will continue to rely on this waiver in their related future dealings with respect to the transaction contemplated hereby and (ii) further warrants and represents that each has reviewed this waiver with its legal counsel, and that each knowingly and voluntarily waives its jury trial rights following consultation with legal counsel. THIS WAIVER IS IRREVOCABLE, MEANING THAT IT MAY NOT BE MODIFIED EITHER ORALLY OR IN WRITING (OTHER THAN BY A MUTUAL WRITTEN WAIVER SPECIFICALLY REFERRING TO THIS SECTION 4.9 AND EXECUTED BY GUARANTIED PARTY AND GUARANTOR), AND THIS WAIVER SHALL APPLY TO ANY SUBSEQUENT AMENDMENTS, RENEWALS, SUPPLEMENTS OR MODIFICATIONS TO THIS GUARANTY. In the event of litigation, this Guaranty may be filed as a written consent to a trial by the court.

4.10 No Other Writing. This writing is intended by Guarantor, Trustee and each Noteholder as the final expression of this Guaranty and is also intended as a complete and exclusive statement of the terms of their agreement with respect to the matters covered hereby. No course of dealing, course of performance or trade usage, and no parol evidence of any nature, shall be used to supplement or modify any terms of this Guaranty. There are no conditions to the full effectiveness of this Guaranty.

4.11 Further Assurances. At any time or from time to time, upon the request of Trustee, Guarantor shall execute and deliver such further documents and do such other acts and things as Trustee may reasonably request in order to effect fully the purposes of this Guaranty.

4.12 Trustee as Agent.

(a) Trustee has been appointed to act as Trustee hereunder by the Noteholders. Trustee shall be obligated, and shall have the right hereunder, to make demands, to give notices, to exercise or refrain from exercising any rights, and to take or refrain from taking any action, solely in accordance with this Guaranty and the Indenture.

(b) Trustee shall at all times be the same Person that is Trustee under the Indenture. Written notice of resignation by Trustee pursuant to Section 8.10 of the Indenture shall also constitute notice of resignation as Trustee under this Guaranty; removal of Trustee pursuant to Section 8.10 of the Indenture shall also constitute removal as Trustee under this Guaranty; and appointment of a successor Trustee pursuant to Section 8.10 of the Indenture shall also constitute appointment of a successor Trustee under this Guaranty. Upon the acceptance of any appointment as Trustee under Section 8.10 of the Indenture by a successor Trustee, that successor Trustee shall thereupon succeed to and become vested with all the rights, powers, privileges and duties of the retiring or removed Trustee under this Guaranty, and the retiring or removed Trustee under this Guaranty shall promptly (i) transfer to such successor Trustee all sums held hereunder, together with all records and other documents necessary or appropriate in connection with the performance of the duties of the successor Trustee under this Guaranty, and (ii) take such other actions as may be necessary or appropriate in connection with the assignment to such successor Trustee of the rights created hereunder, whereupon such retiring or removed Trustee shall be discharged from its duties and obligations under this Guaranty. After any retiring or removed Trustee's

resignation or removal hereunder as Trustee, the provisions of this Guaranty shall inure to its benefit as to any actions taken or omitted to be taken by it under this Guaranty while it was Trustee hereunder.

IN WITNESS WHEREOF, Guarantor has caused this Guaranty to be duly executed and delivered by its officer thereunto duly authorized as of the date first written above.

TOTAL RENAL CARE HOLDINGS, INC.

By:

Name:

Title:



## SUBSIDIARIES OF THE COMPANY

NAME	STRUCTURE	JURISDICTION OF INCORPORATION
Astro, Hobby, West MI., Renal Care Limited Partnership	Limited Partnership	DE
Bay Area Dialysis Partnership	Partnership	CA
Beverly Hills Dialysis Partnership	Partnership	CA
Burbank Dialysis Partnership	Partnership	CA
Caper S.A.	Sociedad Anonima*	(1)
Capital Dialysis Partnership	Partnership	CA
Carroll County Dialysis Facility, Inc.	Corporation	MD
Carroll County Dialysis Facility Limited Partnership	Limited Partnership	MD
Centro Modelo Privado de Enfermedades Renales S.A.	Sociedad Anonima*	(1)
CERCOS S.R.L.	Sociedad de Responsabilidad Limitada	Italy
Continental Dialysis Center, Inc.	Corporation	VA
Continental Dialysis Center of Springfield- Fairfax, Inc.	Corporation	VA
Crescent City Dialysis Center	Partnership	LA
Dialysis Care of North Carolina, L.L.C.	Limited Liability Company	DE
Dialysis Laboratories, Inc.	Corporation	FL
Dialysis Treatment Centers of Macon, L.L.C.	Limited Liability Company	GA
East End Dialysis Center, Inc.	Corporation	VA
Eastmont Partnership	Partnership	CA
Eaton Canyon Dialysis Partnership	Partnership	CA
Enfermedades Renales-- Centro de Dialisis S.A.	Sociedad Anonima*	(2)
ENNE E. S.R.L.	Sociedad de Responsabilidad Limitada	Italy
Flamingo Park Kidney Center, Inc.	Corporation	FL
Garey Dialysis Center Partnership	Partnership	CA
Guam Renal Care Partnership	Partnership	Guam
Guam Renal Management Partnership	Partnership	Guam
Houston Kidney Center/Total Renal Care Integrated Services Network, L.P.	Partnership	DE
Hutchinson Dialysis, L.L.C.	Limited Liability Company	KS
Kenner Dialysis	Partnership	LA

NAME	STRUCTURE	JURISDICTION OF INCORPORATION
Lincoln Park Dialysis Services, Inc.	Corporation	IL
Los Angeles Dialysis Center	Partnership	CA
Mason-Dixon Dialysis Facilities, Inc.	Corporation	MD
Moncrief Dialysis Center/Total Renal Care Limited Partnership	Limited Partnership	DE
Nedial Napoli, S.R.L.	Societa di Responsibilita Limitata	Italy
Nedial, S.R.L.	Societa di Responsibilita Limitata	Italy
Nudial S.A.	Societa Anonima*	(3)
Open Access Sonography Pacific Coast Dialysis Center	Corporation	FL
Pacific Dialysis Partnership	Partnership	CA
Peninsula Dialysis Centers, Inc.	Partnership	Guam
Raquemar S.A.	Corporation	VA
Renal Diagnostic Laboratories, Inc.	Societa Anonima	(3)
Renal Treatment Centers-- California, Inc.	Corporation	DE
Renal Treatment Centers-- Hawaii, Inc.	Corporation	DE
Renal Treatment Centers-- Illinois, Inc.	Corporation	DE
Renal Treatment Centers, Inc.	Corporation	DE
Renal Treatment Centers-- Management Acquisition, Inc.	Corporation	DE
Renal Treatment Centers-- Mid-Atlantic, Inc.	Corporation	DE
Renal Treatment Centers-- Northeast, Inc.	Corporation	DE
Renal Treatment Centers-- Southeast, Inc.	Corporation	DE
Renal Treatment Centers-- West, Inc.	Corporation	DE
RTC Argentina S.A.	Corporation	(3)
RTC Buenos Aires S.A.	Societa Anonima	(3)
RTC Cordoba S.A.	Societa Anonima	(3)
RTC Holdings, Inc.	Corporation	DE
RTC Holdings International, Inc.	Corporation	DE
RTC Supply, Inc.	Corporation	DE
RTC--Texas Acquisition, Inc.	Corporation	DE
RTC TN, Inc.	Corporation	DE
San Gabriel Valley Partnership	Partnership	CA
Servicio De Nefrologia Del Hospital Regional Espanol De Bahia Blanca S.A.	Societa Anonima	(4)

NAME	STRUCTURE	JURISDICTION OF INCORPORATION
Servicio Integral De Nefrologia Y Hemodialisis S.A.	Sociedad Anonima	(4)
Southwest Dialysis Center, Inc.	Corporation	TX
Sunrise Dialysis Partnership	Partnership	CA
Theradial S.A.	Sociedad Anonima	(4)
Tomball Dialysis, Inc.	Corporation	TX
Total Acute Kidney Care, Inc.	Corporation	FL
Total Nephrology Care Network Medical Associates, Inc.	Corporation	CA
Total Renal Care (UK) Limited	Corporation	(4)
Total Renal Care Acquisition Corp.	Corporation	DE
Total Renal Care/Crystal River Dialysis Center, L.L.C.	Limited Liability Company	FL
Total Renal Care Hollywood Partnership	Partnership	CA
Total Renal Care, Inc.	Corporation	CA
Total Renal Care International Limited	Corporation	(5)
Total Renal Care of New York, Inc.	Corporation	NY
Total Renal Care of Puerto Rico, Inc.	Corporation	Puerto Rico
Total Renal Care of Utah, L.L.C.	Limited Liability Company	DE
Total Renal Care/Peralta Renal Center	Partnership	CA
Total Renal Care/Piedmont Dialysis Center	Partnership	CA
Total Renal Care Texas Limited Partnership	Limited Partnership	DE
Total Renal Care West, Inc.	Corporation	DE
Total Renal Italia, S.R.L.	Sociedad de Responsabilidad Limitada	Italy
Total Renal Research Institute, Inc.	Corporation	DE
Total Renal Support Services, Inc.	Corporation	DE
Total Renal Support Services of North Carolina, L.L.C.	Limited Liability Company	DE
TRC El Paso Limited Partnership	Limited Partnership	DE
TRC-Petersburg, L.L.C.	Limited Liability Company	DE
TRC-Rogosin Group, L.P.	Limited Partnership	NY
Tri-City Dialysis Center, Inc.	Corporation	VA
Unidad Modelo de Nefrologia y Hemodialisis S.A.	Sociedad Anonima*	(1)
University Park Dialysis	Partnership	CA
University Park Dialysis Partnership	Partnership	CA
Wilshire Dialysis Center	Partnership	CA

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(1) Cordoba, Province of Cordoba, Argentina

(2) Mendoza, Province of Mendoza, Argentina

(3) City of Buenos Aires, Argentina

(4) Argentina

(5) United Kingdom

\* These entities were each originally a Sociedad de Responsabilidad Limitada (S.R.L.), but were each transformed into a Sociedad Anonima prior to acquisition by RTC Argentina S.A. The transformation in each case is still in the process of being registered before the applicable Public Register of Commerce.

CONSENT OF INDEPENDENT ACCOUNTANTS

We hereby consent to the incorporation by reference in the Statements on Form S-8 (No. 33-84610, No. 33-83018, No. 33-99862, No. 33-99864, No. 333-1620, No. 333-34693, No. 333-34695, No. 333-42653 and No. 333-46887) of Total Renal Care Holdings, Inc. of our report dated February 16, 1998, except as to Note 17 which is as of March 30, 1998, appearing on page F-1 in this Annual Report on Form 10-K. We also consent to the incorporation by reference of our report on the Financial Statement Schedules, which appears on page S-1 of this Form 10-K.

Price Waterhouse LLP

Seattle, Washington  
March 30, 1998



YEAR			
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	JAN-01-1997		
	DEC-31-1997		
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