Innovating for a better life.

1998 Annual Report

Fresenius Medical Care

Contacts

Fresenius Medical Care AG
D-61346 Bad Homburg v.d.H.
http://www.fmc-ag.com

Investor Relations
Petra Kugler
Tel. +49 (6172) 609-2525
Fax +49 (6172) 609-2301
e-mail: ir-fms@fmc-ag.com

In North America:
Heinz Schmidt
Tel. +1 (781) 402-4518
Fax +1 (781) 402-9741
e-mail: ir-fmcna@fmc-ag.com

Public Relations
Oliver Heieck
Tel. +49 (6172) 609-2101
Fax +49 (6172) 609-2294
e-mail: pr-fms@fmc-ag.de

Transfer Agent
ADR Service Center
P.O. Box 8205
Boston, MA 02266-8205
USA
Tel. (800) 428-4237
(toll-free number in the U.S.)
Tel. +1 (781) 575-4328
(for callers outside the U.S.)

Financial Calendar 1999

May 4	**First Quarter 1999** Earnings Release
June 2	**Annual Shareholders' Meeting** Kurhaus, Bad Homburg v.d.H., Germany
June 4	**Dividend Payment**
August 3	**Second Quarter 1999** Earnings Release
November 2	**Third Quarter 1999** Earnings Release

Press announcements are available on the internet on the day of the release under http://www.fmc-ag.com

Published by:
Fresenius Medical Care AG
Investor Relations

This annual report is also available in German
Dieser Geschäftsbericht erscheint auch in deutscher Sprache

Concept and Design: Liebchen + Liebchen GmbH, Frankfurt am Main, Germany

Fresenius Medical Care sets superior standards in renal patient care through its commitment to developing innovative dialysis products and therapies.

We offer a complete product range for both treatment modalities – hemodialysis and peritoneal dialysis – and are the world's largest full-service provider of dialysis care. Our R&D team focuses on maintaining the technological edge that makes innovative products and enhanced therapies possible.

With operations in over 100 countries, we are a truly global company. Our decentralized organizational structure promotes autonomy at the local level while rigorous performance standards ensure maximum efficiency. Close to 29,000 employees are united in their commitment to providing highest quality products and bringing the best medical practices to renal patient care.

Innovating for a better life.

Worldwide, the current dialysis patient population is approximately 920,000. It is expected to continue to grow at 7-9 % annually as thousands of people gain access to life-saving dialysis treatment. We at Fresenius Medical Care remain dedicated to improving the quality of life for dialysis patients and to furthering our leadership in the industry.

Key Figures 1998

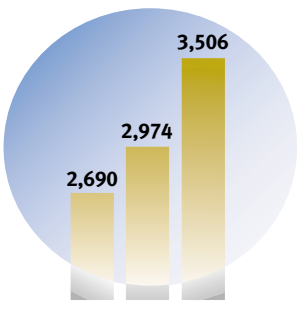
Continuing Operations[1]	1998	1997	1996 pro forma[2]	Change 1998 vs. 1997
Operating data $ in millions				
Net revenue	3,506	2,974	2,690	18 %
Earnings before interest and taxes, depreciation and amortization (EBITDA)	768	641	529[3]	20 %
Earnings before interest and taxes (EBIT)	489	391	285	25 %
Earnings before taxes	269	208	129	30 %
Net income	132	104	48	27 %
Total assets[4]	5,679	5,541	5,093	2 %
Long-term liabilities[4]	2,347	2,225	2,058	5 %
Capital expenditures	159	209	152	- 24 %
Acquisitions	265	527	94	- 50 %
Depreciation and amortization	279	250	214	11 %
Free cash flow[5]	135	59	n.a.	129 %
Data per share				
Earnings per ordinary share (in $)	1.62	1.34	0.51	21 %
Earnings per ordinary ADR (in $)	0.54	0.45	0.17	21 %
Dividend per ordinary share (in DM)	1.15	1.00	0.00	15 %
Dividend per preference share (in DM)	1.25	1.10	0.20[6]	14 %
Key ratios				
EBITDA margin (in %)	21.9	21.6	19.7	
EBIT margin (in %)	13.9	13.1	10.6	
Return on equity before taxes (in %)	11.4	8.5	6.0	
Equity to assets[4] (in %)	41.5	44.1	42.3	
Other data				
Number of employees (Dec. 31)[7]	28,739	28,019	25,789	3 %
Millions of dialysis treatments performed	10.5	9.1	n.a.	16 %

unaudited

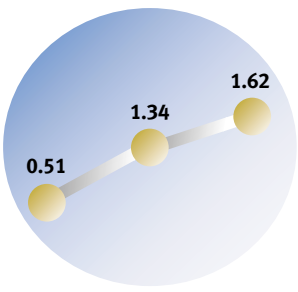
1) Excluding divested businesses
2) As if the merger creating the company had been effective as of January 1, 1996
3) Excluding non-recurring items
4) 1996 figures including divested businesses
5) Before acquisitions and dividends
6) Distributed in 1998
7) 1998 figure excluding divested businesses; 1997 and 1996 figures including divested businesses

All charts included in this report refer to continuing operations with 1996 on a pro forma basis

Net Revenue
$ in millions

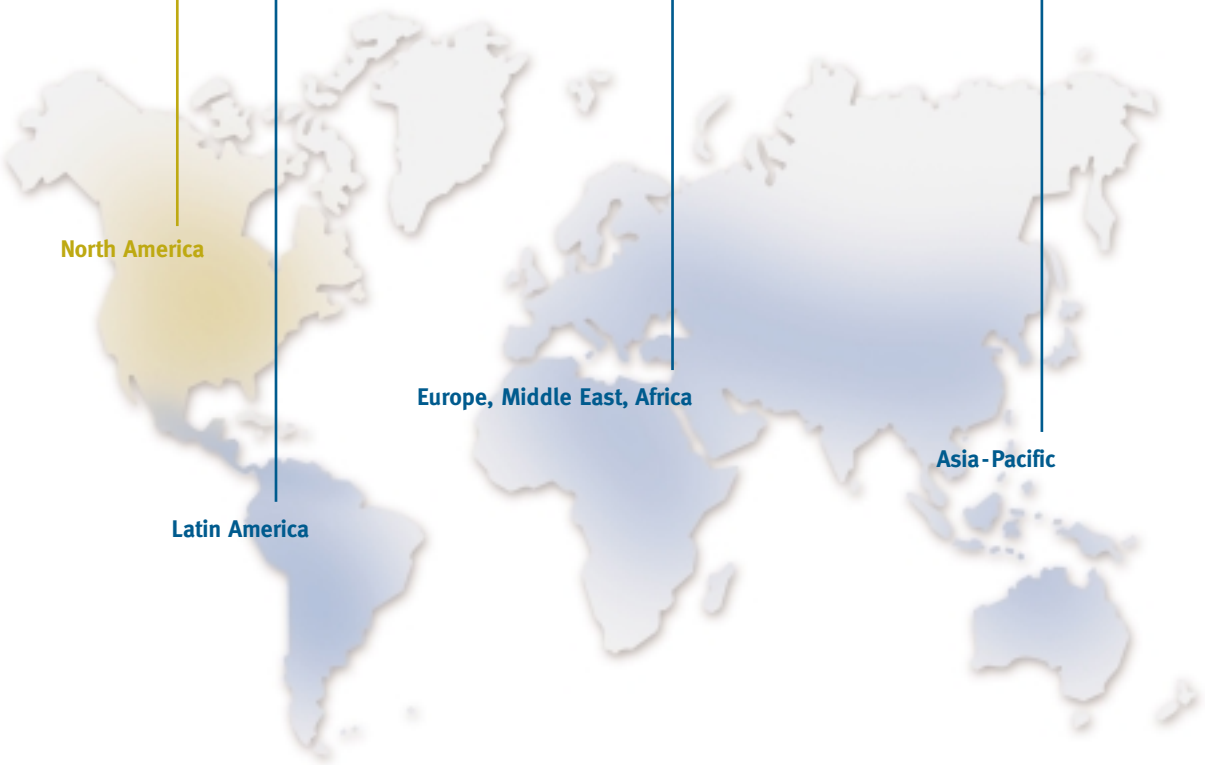


Earnings per Share
in $



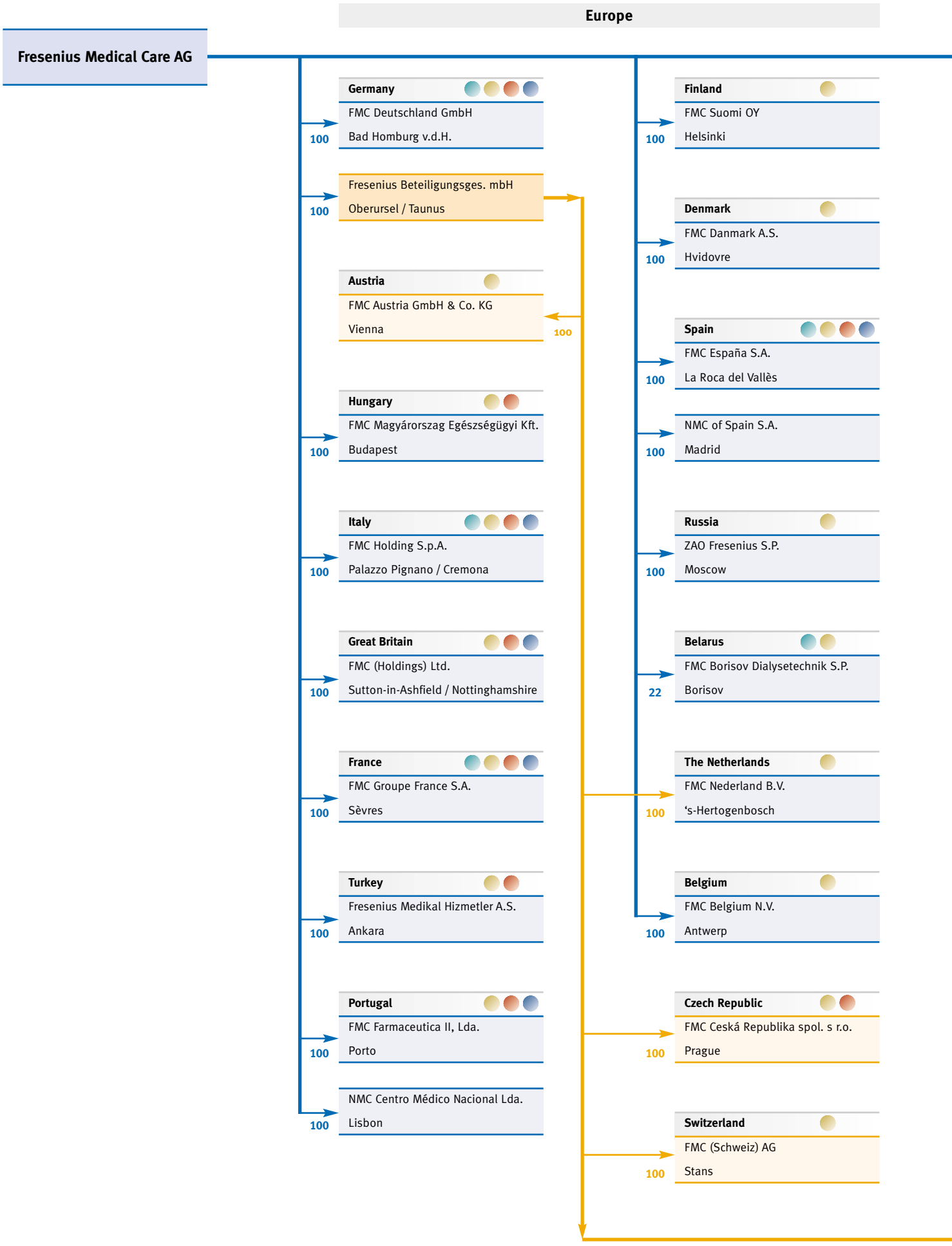
Regional Revenue Structure

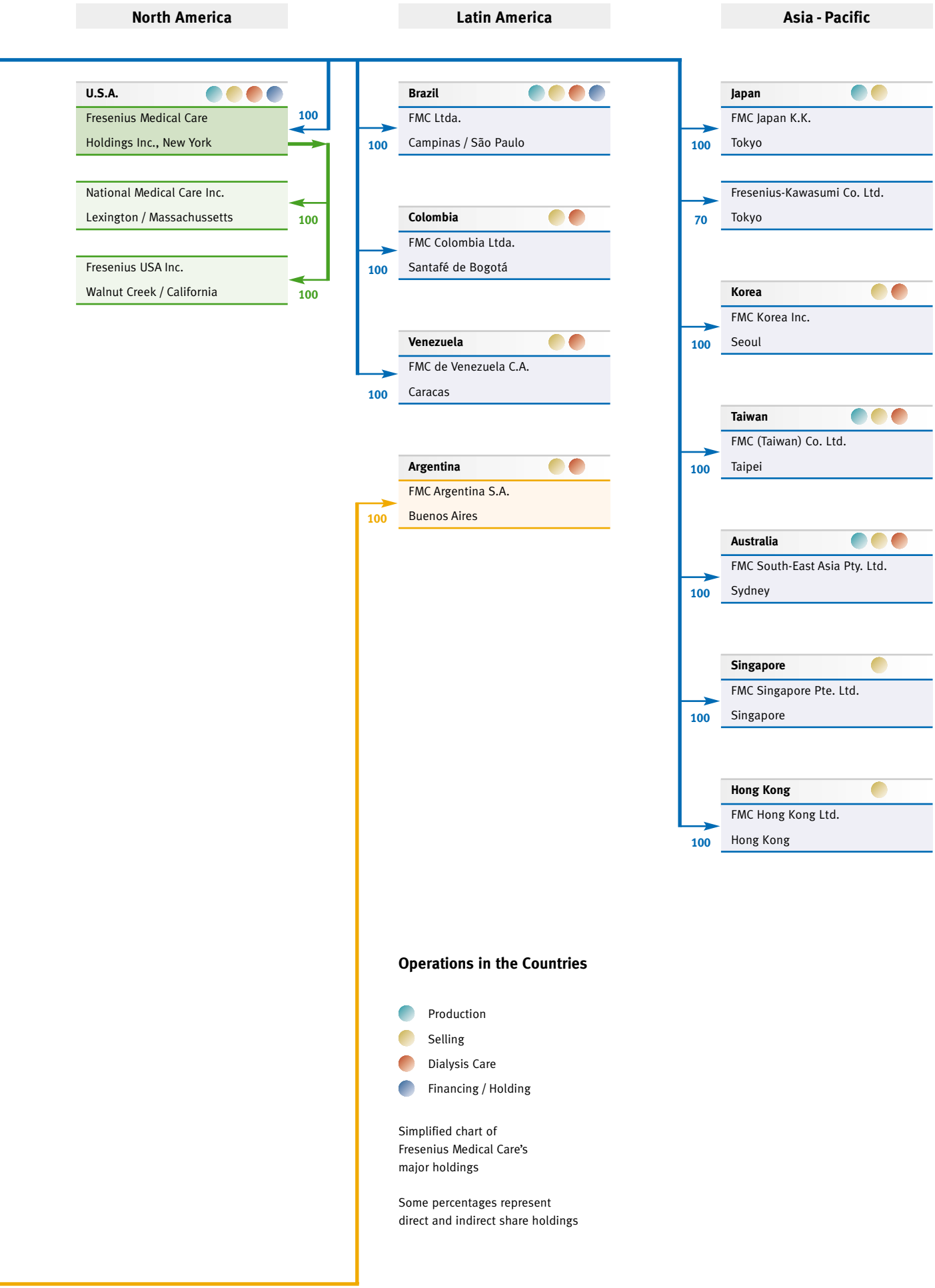
	Segments	
	North America *73 % of total revenue*	**International** *27 % of total revenue*
Dialysis Products Complete range of products for hemodialysis and peritoneal dialysis *33 % of total revenue*	18 %	74 %
Dialysis Care Treatment of patients with acute and chronic kidney failure *67 % of total revenue*	82 %	26 %
	100 %	100 %



Over 74,200 patients – 8 % of global patients – treated in 1,000 FMC clinics

Fresenius Medical Care's Major Holdings





Simplified chart of
Fresenius Medical Care's
major holdings

Some percentages represent
direct and indirect share holdings

Contents

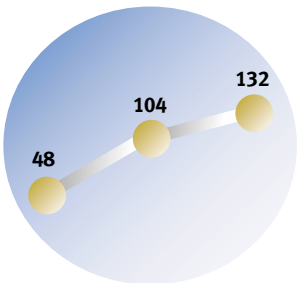
Letter to our Shareholders

To our Shareholders:

1998 was another eventful year for Fresenius Medical Care. Over the course of the year, we further strengthened our leading position in the global dialysis market, focused our attention on our core dialysis business by divesting under-performing assets and continued to exploit the full potential of synergies we envisioned from the merger with National Medical Care in late 1996. These efforts resulted in record revenue and net income and provide a solid foundation for further improvements in the years ahead.

To ensure that Fresenius Medical Care remains at the forefront of our industry, we continued to invest in research and development as well as in our manufacturing facilities. We also furthered our commitment to disease state management in North America through innovative partnerships that allow Fresenius Medical Care to provide a wider range of dialysis-related services to our patients. The concept of disease state management aims at taking into account all medical aspects and the total cost associated with the treatment of a dialysis patient instead of the currently prevailing reimbursement on a fee-for-service basis. The ultimate goal of everything we do is to ensure that our patients receive the highest quality care possible.

Net Income
$ in millions



A Year of Record Results

Our financial performance in 1998 improved significantly compared to the prior year. Led by very strong growth in global markets, total revenue from the segments North America and International with their businesses Dialysis Products and Dialysis Care, reported as continuing operations, increased 18 percent to $ 3.5 billion. During 1998, both our Dialysis Products and Dialysis Care businesses grew at rates well in excess of their respective markets. Net income from continuing operations grew even faster than revenue, increasing 27 percent to $ 132 million. As previously announced, we divested the non-core businesses Homecare and Diagnostics in North America. Although these divestitures resulted in a loss of $ 106 million after taxes, which substantially reduced reported net income from total operations, results since the sale of these under-performing operations have improved notably – a trend that we expect to continue going forward.

In North America, by far our largest market with 73 % of total revenue, we clearly outpace our competitors both in terms of patients treated and products. During 1998, we opened 52 de novo clinics and acquired 24 clinics in selected regions of North America. Our unique clinical information system, which provides access to a vast warehouse of critical patient data, is now operational across the continent. It will enable us to better manage patient care, thereby improving outcomes and the overall level of care provided to all of our patients.

In contrast to the North American segment, the majority of the International segment's revenue is currently derived from dialysis products sold in the various regions. Reflecting continuous innovation and our commitment to superior therapies, the International Dialysis Products' business has

consistently gained market share over the past years. Increasingly, we are focused on expanding our Dialysis Care activities in the International segment. During 1998, 39 clinics were acquired, mainly in Europe and Latin America, and five de novo clinics were opened. The acquisitions completed in 1997 allowed for substantial increases in revenue and treatments.

When compared to the previous year's number of treatments, Fresenius Medical Care achieved a substantial increase of 16 percent.

In line with our earnings-driven dividend policy, the Managing Board and the Supervisory Board propose to the Annual Shareholders' Meeting that the dividend payment be DM 1.15 for ordinary shares and DM 1.25 for preference shares. This represents an increase over the previous year of 15 percent and 14 percent respectively.

Growing Stronger Financially

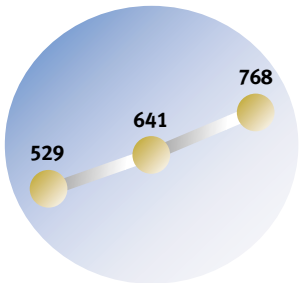
The favorable trend in reimbursement in the U.S. coupled with efficient cost control contributed to a strengthening in margins which trended upward as the year progressed. Earnings before interest, taxes, depreciation and amortization (EBITDA), an important indicator of the financial strength of our ongoing operations, increased 20 percent to $ 768 million in 1998. Thus, cash generated by our continuing operations will provide us with the financial flexibility to fund future growth as well as to meet the obligations of our long-term debt program. Opening new clinics to expand our existing network and making selective acquisitions in areas with attractive reimbursement are among the uses we envision for our growing cash flow. Although our balance sheet is strong, we plan to further improve our debt to EBITDA ratio. Our primary financial goal is for earnings per share growth to clearly exceed revenue growth rate.

Market Dynamics Support Continued Growth

The worldwide dialysis patient population continues to grow between seven and nine percent annually fueled by an aging population, increased incidence of diseases associated with renal complications, improved dialysis treatment methods and general economic growth in the less industrialized regions of the world. Patient growth in some areas, notably Latin America and Asia-Pacific, excluding Japan, is currently much higher than the global average. Based on the financial opportunities, we have focused resources on building a presence in these markets and we intend to continue to develop these markets. The increase of our stake in Fresenius Kawasumi, our Japanese joint venture, from 50 to 70 percent provides us with a good basis to significantly increase our sales of dialyzers in this important market. The appointment of a board member responsible for Asia-Pacific further underscores our commitment to expand our activities in this area.

In addition to the anticipated growth in the patient population, we see opportunities for us as a vertically-integrated company to benefit from the growing shift in ownership of clinics from the public to the private sector. Thus, more of the market becomes available to chain providers like Fresenius Medical Care. The trend towards consolidation that has characterized the North American market for the past few years is spreading to other areas of the world. Our experience in North America will serve us well as we continue to gain shares in key international markets.

EBITDA
$ in millions



Vertical Integration Enhances Market Position

Fresenius Medical Care now treats over 74,200 patients in 1,000 clinics around the world, nearly twice as many as our nearest competitor. In addition to the economies of scale that sheer size allows, our ability to offer complete solutions by combining products with services provides a clear competitive advantage. Our dedication to innovation in dialysis products combined with our outcome-focused approach in dialysis care leads to superior, cost-effective therapies and ultimately a higher life-expectancy for our patients.

Controlling our own destiny through vertical integration also results in predictable product costs over the long term, an important consideration for any healthcare provider, as we face continuous pressure to control costs. With an established presence in over 100 countries, our Dialysis Products business also provides a platform for further growth in our Dialysis Care business.

Fresenius Medical Care has a long history of successful new product introductions, and the past year was no exception. A number of important product innovations were launched in the fields of hemodialysis and peritoneal dialysis.

Leading the Industry in Disease State Management

We continue to believe that payors in the U.S. will increasingly look to capitated risk-sharing arrangements as they seek to manage costs and provide high-quality care for the growing number of patients with chronic kidney failure. Fresenius Medical Care is at the forefront of this emerging trend. By the end of 1998, Fresenius Medical Care had approximately 800 patients in disease state management projects, largely in co-operation with our joint venture partner Kaiser Permanente, the largest health maintenance organization in the U.S. In the second half of 1998, we entered vascular access management with Renaissance, our joint venture with nephrologists. This dialysis-related service not only provides attractive revenue opportunities, but also helps us reduce the hospitalization cost for the patients – a factor gaining in importance as the market moves towards capitated reimbursement.

Outlook for Growth Remains Strong

Our market remains dynamic and, as the world's largest, fully integrated provider of dialysis products and dialysis care, Fresenius Medical Care has distinct competitive advantages. As we enter 1999, we see opportunities for growth around the world and a company with the human and financial resources to capitalize on these opportunities. We believe that revenue can increase by 10 percent in 1999, excluding acquisitions, and that net income can grow at a much faster pace than revenue. The Company's management clearly aims to increase the value of the Company, thereby creating shareholder wealth. To ensure that management's interests are aligned with those of our shareholders, managers have traditionally received a profit-linked remuneration as a variable portion of their total compensation. Since 1998 this variable portion has been extended by the introduction of stock

options. Also, employees participate in the Company's profits to promote their entrepreneurial spirit. The qualifications of our employees ensure the success of our Company, now and in the future. In addition to promoting professional knowledge, selected educational programs focus on leadership and managerial skills.

We are proud of our accomplishments in 1998, which were made possible by the dedication and hard work of almost 29,000 employees and our business partners around the world, and we gratefully acknowledge their contribution to our performance. We also thank you, our shareholders, for your continued support.

Udo Werlé
Chairman of the Managing Board

from left to right:

Hans-Ulrich Sutter
Roberto Fusté
Udo Werlé
Dr. Ben Lipps
Dr. Emanuele Gatti

Strategy

Our mission is to set superior standards in renal patient care through our commitment to developing innovative dialysis products and therapies. Our strategy flows from this commitment to 'Innovating for a better life' for our patients as well as from our obligation to create value over the long term for our shareholders.

Hemodialysis treatment in a U.S. clinic

Key elements of our growth strategy include:

Focus on Dialysis Products and Dialysis Care
Following the sale of the non-renal businesses in 1998, in both segments we are firmly focused on Dialysis Products and Dialysis Care, areas where we have over 25 years of extensive experience.

Expand Leadership Position
Expected growth in the number of dialysis patients coupled with the continued consolidation of our industry provides the opportunity to expand our leading position in both Dialysis Products and Dialysis Care in all regions of the world. The different needs of the local markets are addressed by our local managers who have the full responsibility for the entire operations in a particular region. Expansion of Dialysis Care, which is the objective in many of our global markets, is driven by a selective approach. We focus on countries with stable reimbursement and on acquisitions that make strategic sense and that meet our strict financial hurdle rates. To take advantage of the growing trend towards consolidation outside of the U.S., we envision making acquisitions in selected international markets. Acquisitions to complement our existing network in North America are also contemplated.

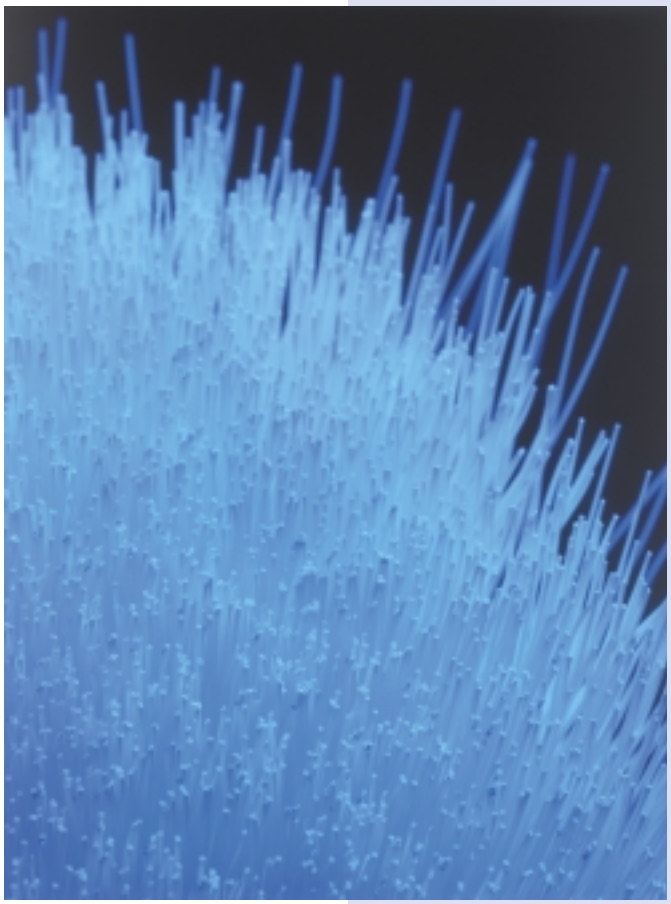
Innovation through Research and Development
Fresenius Medical Care will continue to pursue intensive research and development aimed at improving treatment outcomes by developing new and enhanced products and therapies.

Maintain Strict Cost Controls
To ensure an appropriate level of profitability in a market characterized by constant price pressure, we continually strive to increase efficiency and to lower costs.

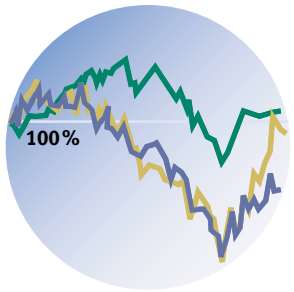
Focus on Internal Growth
Going forward, our focus is on generating internal growth that exceeds market growth and allows for earnings to increase at a faster pace than revenue.

Actively Promote Market Changes
We are prepared to meet the changing demands of the marketplace. In 1999 and beyond, capitated risk-sharing arrangements are expected to gain increased acceptance, particularly in the U.S., where payors are intently focused on reducing the cost of care. This trend creates an opportunity for the Company to assume a far greater share of the total spectrum of care for the renal patient. Through several unique joint ventures, Fresenius Medical Care North America is already leading the industry in disease state management.

Fresenius Polysulfone®
membrane



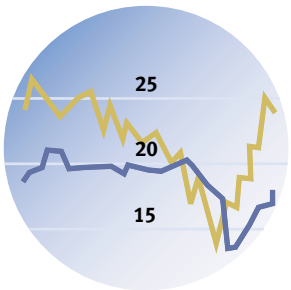
Share Price
Frankfurt Stock Exchange



Jan. 4 1998 Dec. 30

Ordinary share
Preference share
German mid-cap index (MDAX)

ADR Share Price
New York Stock Exchange



1998

Closing Price in $
Ordinary ADR
Preference ADR

Ticker Symbols

Frankfurt Stock Exchange (FSE)	
Ordinary share	FME
Preference share	FME3

New York Stock Exchange (NYSE)	
Ordinary ADR	FMS
Preference ADR	FMS.Pr

Fresenius Medical Care ranks among the top 35 German listed companies by trading volume and is among the top 50 companies by market capitalization on the German stock exchange. Fresenius Medical Care was one of the first German companies to list its shares on the New York Stock Exchange (NYSE), the world's premier stock exchange.

Since the formation of the Company, Fresenius Medical Care's ordinary shares have been included in the German mid-cap index MDAX and, since its creation, the STOXX, a pan-European index that comprises some 650-plus major European companies. On the NYSE, both ordinary and preference shares are traded in the form of American Depositary Receipts (ADRs), with one share equivalent to three ADRs. The U.S. listing clearly reflects the Company's commitment to the North American market, where it generates over 70 % of its revenue. On average, over 23 million ADRs were outstanding during 1998.

Turbulent Financial Markets in 1998
The global financial markets were extremely volatile throughout 1998. Following unexpected cuts in interest rates and large inflows of new capital, the stock markets both in Europe and the U.S. registered record highs in the middle of the year. The DAX, an index representing Germany's 30 largest listed companies, reached its new all time high of 6,224.52 points on July 21. Its counterpart in the U.S., the Dow Jones Industrial Average, also recorded an all time high at approximately the same time.

In August, the financial crises in Asia and Russia, coupled with financial turmoil in emerging markets, caused fears of a global recession. The near collapse of a large and highly leveraged U.S. hedge fund raised further concern about the financial health of similar funds, which are largely unregulated. A cut in U.S. interest rates in October had a stabilizing effect on the markets, which allowed a resurgence of share prices and a new high in the Dow Jones Industrial Average.

In 1998, the DAX rose by 19 % and the index representing Germany's 70 biggest mid-caps, the MDAX, rose by 7 %. The Dow Jones climbed 16 % for the year while the S&P 500 rose 27 %.

Share Price Performance
Until the last quarter of 1998, the performance of Fresenius Medical Care's shares lagged behind that of the overall market. Fresenius Medical Care's third quarter results announced in November helped to regain investors' confidence and was followed by a recovery in the share price. The Fresenius Medical Care shares outperformed the overall market through the remainder of the year.

The ordinary shares closed at € 60.08 at the end of the year, with a loss of 0.2 % compared to the beginning of the year. The preference shares closed at € 38.86, a loss of 28 % over the year – despite outperforming the overall market during the last three months of the year. Reflecting the adoption of a single currency by the European Monetary Union, Fresenius Medical Care's shares have been quoted in euros since January 4, 1999.

The preference shares are non-voting, but bear a higher dividend compared to the ordinary shares. Stock options as well as performance-based earnings for employees are linked to preference shares.

The ordinary ADRs closed the year at $ 23.50, having rebounded from a low of $ 12.50 earlier in the year. For the year, the ordinary ADRs rose 8 %. The preference ADRs closed at $ 16.13 at year end, representing a loss of 10 %.

Dividend Raised
In line with our earnings-driven dividend distribution policy, our shareholders will participate in the Company's favorable financial performance in 1998. The Managing Board and Supervisory Board propose to the Annual Shareholders' Meeting that a dividend of DM 1.15 per ordinary share and DM 1.25

per preference share will be paid for the 1998 fiscal year. This represents an increase of 15 % for the ordinary shares and 14 % for the preference shares over the previous year. The total dividend distribution amounts to $ 52 million or 40 % of the Group's net income for the year.

Investor Relations

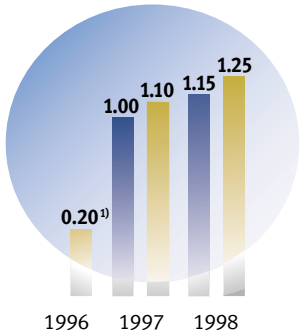
The objective of our Investor Relations activities is to ensure open, timely and comprehensive communication with shareholders and the financial community. The aim of our ongoing communication is to reinforce the confidence of our shareholders and potential investors as well as to enable financial analysts to adequately evaluate the Company.

During 1998, the management of Fresenius Medical Care visited a number of large financial centers both in Europe and the U.S., a reflection of increased interest in the Company as well as our efforts to increase the Company's visibility in the financial community. Shareholders also have access to Company information via our website *(http://www.fmc-ag.com)*, where news releases are always accessible immediately.

The Investor Relations department in the North American headquarters in Lexington, Massachusetts, assures equally timely and comprehensive access to Company information for our U.S. shareholders and U.S.-based analysts.

Our program of active communication with the financial community in both Europe and the U.S. will be further intensified in 1999.

Dividend per Share
in DM

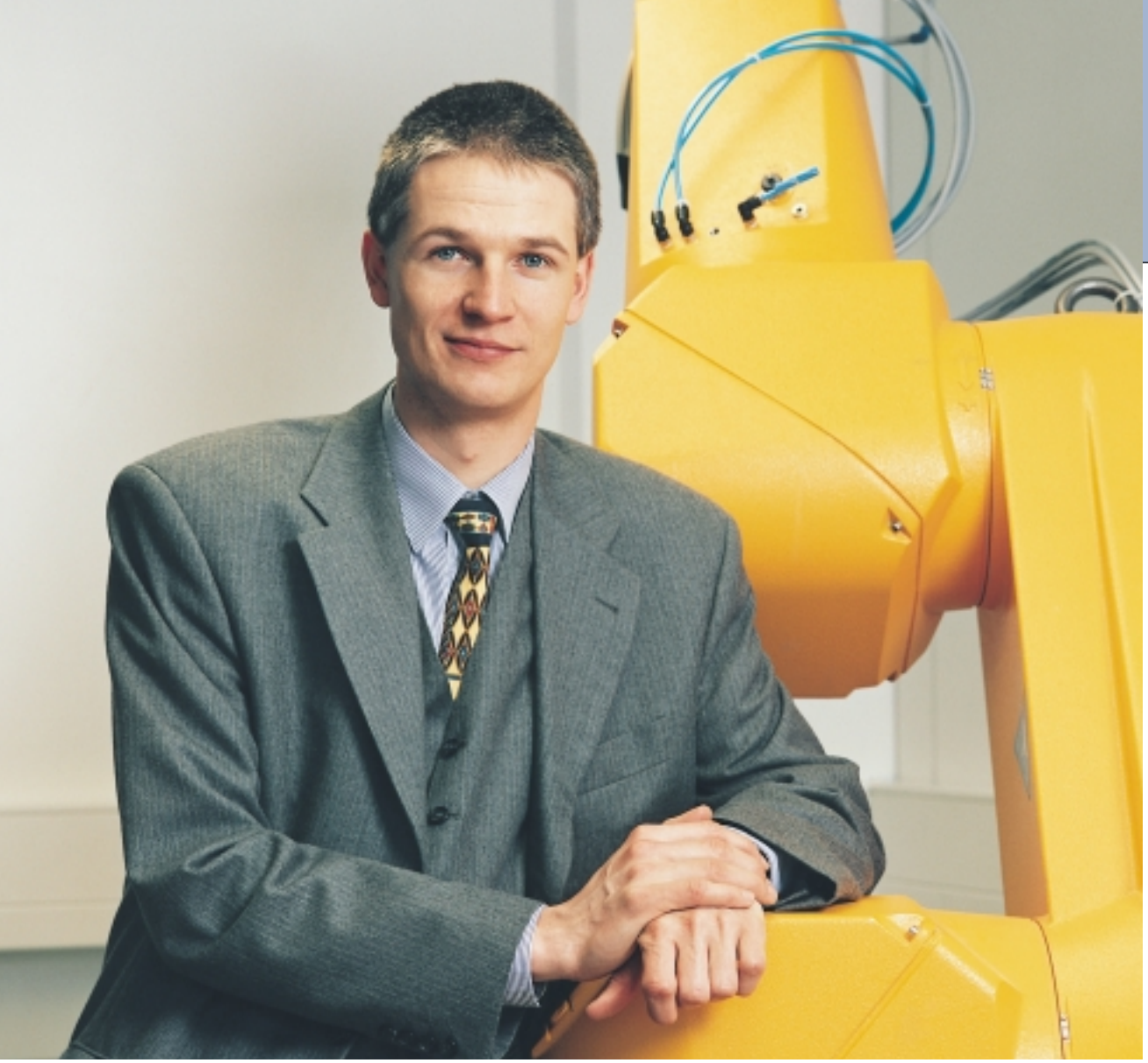


1) Distributed in 1998

		1998		1997		1996	
		Ordinary	Preference	Ordinary	Preference	Ordinary	Preference
Number of shares (nominal value DM 5)	million	70	9.02	70	9.02	70	5.4
Share price (FSE) 1)							
high	€	72.43	57.26	85.9	71.07	74.39	64.78
low	€	30.68	25.56	55.73	46.02	57.98	62.43
year end	€	60.08	39.63	61.10	49.59	67.34	63.37
Average daily trading volume (FSE)		98,263 2)	14,517 2)	592,000	127,000	414,000	35,000
ADR share price (NYSE) 1)							
high	$	26.875	21.000	31.500	26.750	31.875	27.750
low	$	12.500	12.125	20.438	18.000	21.125	25.875
year end	$	23.500	16.125	21.750	18.000	28.125	26.000
Market capitalization	€ bn	4.56		4.72		5.05	

1) Closing prices

2) Volume according to the new counting rule published by Deutsche Börse AG. According to the old counting rule, the volume for the ordinary shares would have been 445,000 and for preference shares 81,000.



“The technology we develop is not the aim in itself – it is the means to achieve better lives for dialysis patients.”

Dr. Joachim Döpper, Research & Development

Meeting Targets

Economic Background
The world economy was influenced by the financial crisis in Asia and political instability in Russia during 1998. However, the economies of the U.S. and Europe, which are our most important markets, were sufficiently resilient to record positive economic growth during the year.

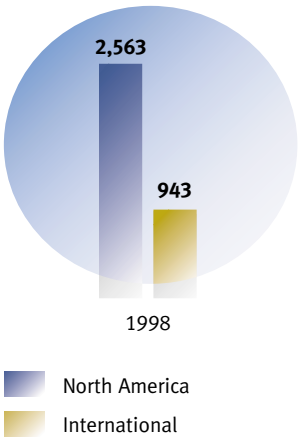
The market for healthcare services and medical products benefited only to a limited extent from the relatively robust global economy. In most industrialized countries, measures to cut healthcare costs or to transfer costs from the public to the private sector characterized the business climate. However, given the steady increase in the number of patients with chronic kidney failure, a population that is growing at a rate of approximately 7-9% per year worldwide, the market for dialysis services and products continues to grow steadily. Two changes in healthcare legislation in the U.S., our biggest market, had a favorable impact on our business. First, the time period during which a patient's private insurance pays for dialysis treatment before Medicare takes over was raised from 18 to 30 months. Second, restrictive reimbursement guidelines for EPO, a drug commonly administered to dialysis patients, were lifted in March. The reimbursement situation outside the U.S. was generally stable.

Even though the average exchange rate of the U.S. dollar, which is the most important currency to Fresenius Medical Care, to the Deutsche Mark increased by just 1% in 1998 compared to the previous year's average, the currency markets were very volatile throughout the year. The dollar closed at 1.67 DM/$ compared to 1.79 DM/$ at the beginning of the year. Exchange rate changes lowered the growth rates in revenue and net income by 0.9 percentage points and 1.6 percentage points respectively. Beyond these translation effects, Fresenius Medical Care has only negligible commercial exposure.

Other than the impact from exchange rate fluctuations, neither the Asian financial crisis nor the crisis in Russia had a serious adverse impact on our business. Within the area Asia-Pacific, Fresenius Medical Care's focus has been on well-developed markets such as Japan, South Korea, Taiwan, Hong Kong and Australia.

Focus on Core Competencies
The divestiture of the U.S. Homecare and Diagnostics businesses in the second half of the year allowed the Company to sharpen its focus on the core Dialysis Products and Dialysis Care businesses. Starting in the second quarter of 1998, the Homecare and Diagnostics businesses were classified as discontinued operations in accordance with U.S. GAAP. A loss of $ 106 million after taxes – of which $ 97 million relates to the sales of the businesses and $ 9 million represents an operating loss – was recorded in the second quarter of 1998. In both its segments the Company is now fully focused on its core Dialysis Products and Dialysis Care businesses, both of which performed very well during 1998 as the following report shows.[1)]

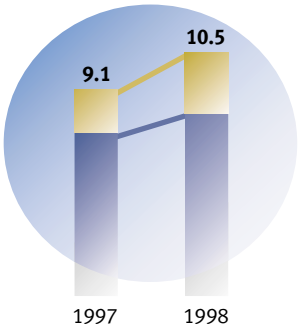
Revenue by Segment
$ in millions



1) All figures are reported in conformity with U.S. GAAP. The numbers exclude discontinued operations and reflect the cumulative effect of an accounting change for start-up costs adopted as of January 1, 1998. The previous years' figures were reclassified to conform to the current period's presentation of continuing operations. Detailed financial statements are included in this report on pages 34-78.

The 1998 Fiscal Year

Number of Treatments
in millions



	1998
International	+ 20%
North America	+ 14%
Total	**+ 16%**

Strong Increase in Revenue
Fresenius Medical Care achieved revenue of $ 3,506 million, an increase of 18 % over 1997. Revenue from continuing operations, excluding acquisitions during the year, increased by 11 %. With 9 % of revenue generated in Germany, 73 % in North America and 18 % in other regions of the world, Fresenius Medical Care is a truly global company.

The strong increase in revenue was driven by solid growth in both segments and both businesses. Revenue from Dialysis Care increased by 24 % to $ 2,359 million in 1998. This growth is largely attributable to an increase in the number of patients under treatment. Selective acquisitions, as well as the opening of new clinics both in North America and internationally, contributed to an increase in the number of dialysis clinics to 1,000 clinics worldwide at the end of the year. In total, over 74,200 patients were treated in Fresenius Medical Care clinics at year end 1998. The number of dialysis treatments rose by 16 % from 1997 to 10.5 million.

Revenue from Dialysis Products' sales to third parties rose by 7 % to $ 1,147 million. As 61 % of sales of Dialysis Products occur outside North America, the strength of the dollar had a negative impact on 1998 product revenue. Based on constant exchange rates, the increase was 9 %, which was once again above market growth. Sales of hemodialysis machines and dialyzers were especially strong during 1998. Including sales of products used in our own dialysis clinics, product sales totaled $ 1,424 million, a 10 % increase over 1997 in constant rates. Our share of the global products market rose significantly in 1998.

Increased Operating Profit
Operating profit, or earnings before interest and taxes (EBIT), was $ 489 million compared to $ 391 million in 1997, up 25 %. The favorable developments in reimbursement in North America combined with a slight improvement in the gross margin and a decline in selling, general and administrative expenses as a percent of revenue resulted in a margin increase of 80 basis points to 13.9 %. Earnings before interest, taxes, depreciation and amortization (EBITDA) increased by 20 % to $ 768 million. The return on revenue based on EBITDA rose from 21.6 % to 21.9 %.

Improved Earnings
Earnings before taxes reached $ 269 million, or 30 % higher than the previous year. Net interest expense was $ 220 million compared to $ 184 million in 1997. The increase in net interest expense over the previous year was primarily attributable to stronger use of the Company's credit facilities to finance acquisitions, which led to an increase in long-term debt. Income tax expense rose to $ 135 million compared to $ 101 million in 1997. The effective tax rate was 50 % in 1998 compared to 49 % in 1997. In 1997 the effective tax rate was lowered by a reduction in valuation allowances for loss carryforwards. Without the change in the valuation allowances, the effective tax rate in 1997 would have been 53 %. After deducting minority interests, the Company's net income was $ 132 million, an increase of 27 % over $ 104 million in 1997. Earnings per share rose by 21 % to $ 1.62. The return on equity before taxes was 11.4 % compared to 8.5 % in 1997.

Abbreviated Statement of Earnings

	1998	1997	Change
Net revenue	3,506	2,974	18 %
Cost of revenue	2,206	1,886	17 %
Gross profit	**1,300**	**1,088**	**20 %**
Selling, general and administrative	780	675	16 %
Research and development	31	22	41 %
Operating income	**489**	**391**	**25 %**
Interest (net)	220	184	20 %
Earnings before income taxes	**269**	**207**	**30 %**
Net income	**132**	**104**	**27 %**
Earnings per share	1.62	1.34	21 %
Earnings per ADR	0.54	0.45	21 %

$ in millions, except share data

Dividend Increased

In line with our earnings-driven distribution policy, shareholders will participate in the Company's improved financial performance in 1998 through an increase in the dividend. The Managing Board and Supervisory Board will propose that shareholders approve a dividend of DM 1.15 per ordinary share and DM 1.25 per preference share, both with a nominal value of DM 5, at the annual shareholders' meeting. This represents an increase of 15 % for the ordinary shares and 14 % for the preference shares over the previous year. The total dividend distribution amounts to $ 52 million calculated at an exchange rate of 1.76 DM/$ or 40 % of net income of $ 132 million for the year.

Capital Expenditures

Fresenius Medical Care's total capital spending amounted to $ 424 million in 1998. Acquisitions, mainly of clinics, accounted for $ 265 million and capital expenditures amounted to $ 159 million.

The majority of the 63 clinics acquired were located outside North America, mainly in Western Europe and Latin America. Investments in fixed assets were primarily dedicated to equipping dialysis clinics as well as opening 57 new clinics to accommodate the increase in patients due to growth in the market. In addition, we made investments in our manufacturing facilities in St. Wendel, Germany, and in Ogden, Utah. At the St. Wendel site, capacity was significantly expanded and in Ogden a new line for dialyzer production commenced operations.

Trust Preferred Securities

Coupon	Issued	Size	Maturity
9.000 %	Nov. 96	$ 360	Dec. 06 [1]
7.875 %	Feb. 98	$ 450	Feb. 08
7.375 %	Feb. 98	DM 300	Feb. 08

Size in millions
1) Earliest optional redemption Dec. 2001

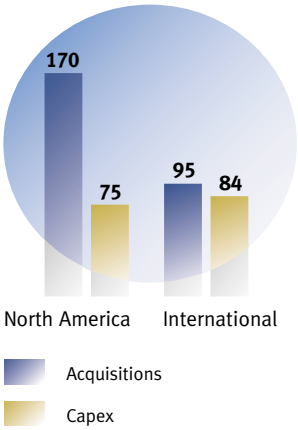
Liquidity and Capital Resources

In February 1998, two tranches of Trust Preferred Securities were issued. The first, in the amount of $ 450 million, was issued by the Fresenius Medical Care Capital Trust II and the second, in the amount of DM 300 million, by the Fresenius Medical Care Capital Trust III. Both issues were exceptionally well received by the capital markets and enabled the Company to strengthen its financial flexibility. $ 250 million of the proceeds were used to repay senior bank debt under the NMC credit agreement. This reduced the credit facility to $ 1.75 billion at the end of 1998. The remaining proceeds of $ 365 million were used to repay other liabilities and for general corporate purposes. Holders of the Trust Preferred Securities are entitled to fixed quarterly distributions at a rate of 7 7/8 % for the dollar-denominated tranche, and at a rate of 7 3/8 % for the DM-denominated tranche and repayment of principal in 2008 at par value. Reflecting the Company's improved financial position, Standard & Poor's upgraded its outlook for Fresenius Medical Care from stable to positive with a B+ rating. The subsequent trading of these securities in the bond market is evidence of the international bond market's high regard for Fresenius Medical Care. In 1998 as a whole, they outperformed the overall market as well as the healthcare segment.

Cash used in investing activities totaled $ 280 million, which was funded by cash from operating activities and by an increase of debt compared to year end 1997. An intercompany loan from the parent company amounted to $ 60 million at year end.

Capital Expenditure and Acquisitions

$ in millions



The 1998 Fiscal Year

Management of Currency and Interest Rate Risks

Derivative financial instruments are used to hedge currency and interest rate risks. These instruments are used solely to protect future payments resulting from the normal business operations of the Company and are only executed with highly regarded banks.

The nominal value of forward currency contracts as of December 31, 1998 was $ 288 million, primarily for hedging Deutsche Mark against U.S. dollars. To hedge the interest rate risk from the Company's senior credit agreement, we entered into various interest swap contracts. The nominal value of these contracts was $ 1.6 billion as of December 31, 1998. These agreements fix the interest rates for the various credit facilities at rates between 5.55% and 6.76 % with expirations running up until January 4, 2005.

Abbreviated Statement of Cash Flows

	1998	1997	Change
Cash at beginning of year	37,818	63,637	n.a.
Cash from operating activities	268,000	194,260	38 %
Cash used in investing activities	(280,266)	(652,849)	-57 %
Cash from financing activities	12,760	424,321	-97 %
Effect of exchange rate on cash	(6,445)	8,449	n.a.
Cash at end of year	31,867	37,818	-16 %

$ in millions

Solid Balance Sheet

As of December 31, 1998, total assets were $ 5.7 billion compared to $ 5.5 billion as of the same date in 1997.[1] Included in total assets is $ 2.8 billion of goodwill, of which 73 % (approx. $ 2.1 billion) relates to the merger of the companies forming Fresenius Medical Care. Total liabilities at December 31, 1998 were $ 3.3 billion. Long-term liabilities increased slightly to $ 2.3 billion from $ 2.2 billion at the end of 1997. Shareholders' equity as of December 31, 1998 amounted to $ 2.4 billion. Working capital was $ 448 million, while the ratio of current assets to current liabilities was 1.5.

Abbreviated Balance Sheets

	Dec. 31, 1998		Dec. 31, 1997	
Assets				
Current assets	1,424	25 %	1,419	26 %
Accounts receivable	638	11 %	534	10 %
Inventories	297	5 %	247	5 %
Other current assets	339	6 %	267	5 %
Discontinued operations	150	3 %	371	6 %
Fixed assets	4,255	75 %	4,122	74 %
Intangible assets	3,484	61 %	3,343	60 %
Other fixed assets	771	14 %	779	14 %
Balance sheet total	**5,679**	**100 %**	**5,541**	**100 %**
Liabilities and shareholders' equity				
Current liabilities	976	17 %	870	16 %
Long-term liabilities	2,346	41 %	2,225	40 %
Shareholders' equity	2,357	42 %	2,446	44 %
Balance sheet total	**5,679**	**100 %**	**5,541**	**100 %**

$ in millions

Manufacturing Operations and Purchasing Management Expanded

In 1998, we reorganized manufacturing operations in our Schweinfurt plant, Germany, where the majority of our dialysis machines are produced, by creating process units dedicated to our main geographic regions. This market-focused structure not only enables us to more actively support the worldwide machine business with the highest responsiveness to the needs of different markets, it also allows us to realize the maximum economies of scale. In addition, the establishment of multi-disciplinary teams has increased productivity, lowered costs and resulted in improved customer service.

1) The assets and liabilities of the Homecare and Diagnostics businesses were classified as 'net assets of discontinued operations'.

Due to the strong demand for our dialysis machines, output rose by 17 % from 12,000 machines in 1997 to 14,000 machines in 1998.

During 1998, capacity was significantly increased in the St. Wendel, Germany, facility by optimizing production processes and implementing more flexible working hours. For example, the changes that were implemented allowed dialyzer and bloodline production capacity to increase by 20 % and 30 % respectively. Various production processes were adapted to meet the more technically complex requirements of our newly developed dialyzers. We also expanded our capacity to produce solutions in non-PVC bags made of Biofine® which is preferable for patients in dialysis treatment. Furthermore, we added another extrusion line to enable a wider array of products to be wrapped in this environmentally-friendly foil. A fully-automated system to measure clearances of dialyzers was developed and implemented in order to enhance fiber production.

In the production facility SMAD in France a production line for Fresenius Polysulfone® dialyzers was put into operation in October of 1998 to meet the growing demand in the European market.

During the first quarter, we expanded production capacity for Fresenius Polysulfone® dialyzers at the plant in Ogden, Utah, which now has the ability to fully meet the market demand in North America.

In mid-1998 a new purchasing department was implemented in the International segment, responsible for a purchasing volume of approximately $ 260 million. Its aim is to realize synergies and cost savings by buying materials of strategic importance with global contracts where possible. Currently, there are 51 international projects in which our worldwide needs are being analyzed and consolidated with a smaller number of preferred suppliers. Raw materials and packaging supplies are two areas of particular focus. We have also begun to standardize parts, materials and processes in conjunction with the areas responsible for marketing, R&D, quality control and logistics in an effort to reduce complexity and increase the flexibility of our manufacturing operations. In North America a similar unit was formed to leverage buying power. The committee selected one office supplies vendor, one national air carrier and one package carrier which all divisions in North America are required to use.

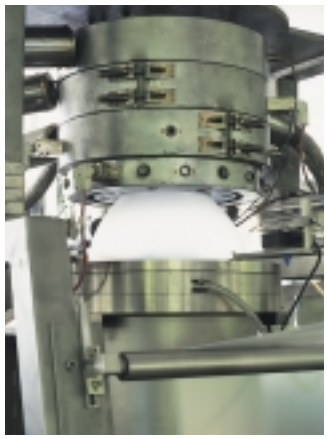
In North America the consolidation of distribution was completed by reducing the number of distribution centers from 38 to 25. This consolidation effort, as well as partnering with major transportation companies, has allowed Fresenius Medical Care to significantly reduce its operating expenses.

With the implementation of SAP/R3 in all countries of Central Europe, the measures initiated in 1997 to achieve cost savings in distribution and logistics were successfully continued. The number of warehouses and overall inventory levels were considerably reduced.

R&D and Marketing Activities

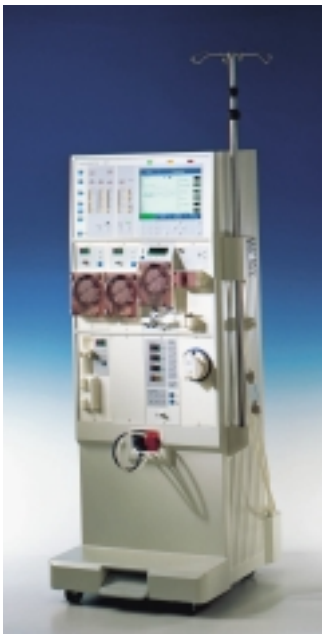
To maintain and further enhance a continuous stream of product innovations, Fresenius Medical Care increased the number of employees working in R&D worldwide to 232 at the end of 1998. Approximately two thirds of the R&D staff is based in Germany.

Total R&D expenditures increased to $ 31 million in 1998, clearly surpassing the $ 22 million spent in the preceding year. This R&D spending represents 3 % of 1998 Dialysis Products' revenue.



Extrusion of Biofine® in St. Wendel, Germany

The 1998 Fiscal Year



4008 H hemodialysis machine with the ONLINE*plus*™ system

In the field of hemodialysis machines, we further expanded our customer-friendly modular systems for individualizing dialysis treatment. The modules launched in 1998 can, for the most part, be used to upgrade previous generations of dialysis machines. In this respect, the new ONLINE*plus*™ system used for hemodiafiltration and hemofiltration launched in mid-1998 is especially noteworthy. To date, hemodiafiltration, which is considered to be the most efficient treatment mode for patients with chronic kidney failure, is used in just a small percentage of all treatments. This is due to the considerable costs associated with the provision of the infusion solution needed for volume substitution. Our ONLINE*plus*™ system uses an innovative process in combination with the specially designed dialysate filter DIASAFE®*plus* to produce the necessary infusion solution during treatment, which is significantly more cost-efficient. The efficacy of the ONLINE*plus*™ system is perfectly complemented by the hemodiafilter H*d*F100S, also launched in 1998, which offers an unmatched capability to eliminate uremic toxins. Using innovation in both process and materials which improves patient care, while at the same time reducing costs, the ONLINE*plus*™ system is evidence of our integrated approach to dialysis therapy.

Fresenius Medical Care is the first producer of dialysis products to obtain the marketing approval from an independent notified body for an active feedback module for controlling the removal of excess fluid from the patient, which is a leading cause of a number of complications during dialysis treatment. The Blood Volume Monitor™ (BVM™) is available as an optional module for all 4008 hemodialysis machines and continuously monitors and controls the removal of fluid from the patient in order to significantly reduce the attendant complications.

In view of the increasing interest in home dialysis, development work continued on a system that allows a technician to monitor the functioning of the *sleep•safe*™ via data transmission. The system will enable technicians to connect to the machines and diagnose possible faults, which optimizes customer service and spare-part stock.

In North America a new method – Online Clearance (OLC) – for measuring the effectiveness of the hemodialysis treatment has been developed and is being released. Once the 2008H dialysis machine is fitted with OLC, a variety of treatment variables critical to patient care and well-being can be assessed at no additional cost. This technique was the subject of clinical trials conducted by the Renal Research Institute, our joint venture with Beth Israel Medical Center. Additional clinical studies were carried out for both the BVM™ and the Blood Temperature Monitor™ (BTM™) in Europe and North America during 1998.

In preparation for the year 2000, our international product lines have been reviewed. Our major products comply with the rules for the year 2000 published by the BSI (British Standards Institution) and the FDA (U.S. Food and Drug Administration). The conversion of older machines still in use, which is necessary in some cases, will be completed in mid-1999 according to plan.

In the area of peritoneal dialysis, Fresenius Medical Care concluded the development of the new *sleep•safe*™ cycler for automated peritoneal dialysis. In 1999, our focus will shift towards clinical trials and field tests in key countries. Launch activities for the *sleep•safe*™ system are planned for the second half of 1999. The cycler, which is primarily used for treatment at home during the night, is characterized by its extremely compact and light design together with a disposable cartridge and a revolutionary pumping mechanism that allows for exact delivery of the peritoneal dialysis solution. Simple and easily understandable prompts from the monitor, as well as an integrated patient management system that supervises and documents the treatment, further enhance the value of the *sleep•safe*™ cycler. New peritoneal dialysis solutions are being developed with the aim of better adapting the solutions to the individual patient's needs.

In 1999, we will continue our renowned R&D efforts for equipment, disposables and software for the benefit of patients and care providers alike. We are looking forward to the introduction of exciting new products for both hemodialysis and peritoneal dialysis that will strengthen our technological leadership in the field.

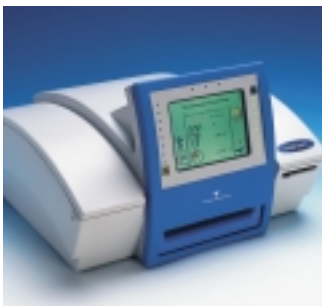
Quality and Environmental Management

In 1998, the corporate quality policy, which puts the health and well-being of the patient at the center of our activities, was implemented. In addition, high standards for environmental protection and safety have been set for the International segment in order to allow for sustainable development. In line with the Company's philosophy of decentralization, each organizational unit and its respective manager have the responsibility along with the authority to achieve the set quality objectives.

The corporate management system is the basis for the CE certification required in the European Union. This was accomplished for all our medical devices well before June 14, 1998, when the applicable European Directive became obligatory. The CE certification proves that our products meet the high European quality standards and can therefore be legally marketed. It further proves that our operating processes from product development to customer service are efficient.

Fresenius Medical Care was the first provider of dialysis care to develop and implement a corporate quality management system in accordance with ISO 9002, which allows the certification of dialysis clinics by an independent notified body. At year end 1998, a total of 20 clinics in four countries achieved this valued recognition.

In North America, all manufacturing facilities continue to operate within all applicable state and federal regulations. The Continuous Quality Improvement Program constitutes a comprehensive approach to addressing not only the clinical aspects, but also technical, organizational and financial operations of the Company. In 1998, we completed our first patient satisfaction survey, which showed a 90 % rate of satisfaction among patients treated by Fresenius Medical Care.



***sleep•safe*™ cycler for peritoneal dialysis**

The 1998 Fiscal Year

Our environmental commitment is evidenced by the certification, according to ISO 14001 and the EU Eco Audit, of various locations of Fresenius Medical Care as well as the creation of a corporate environmental management system in 1998, which can now be certified by an independent institution. Our comprehensive approach starts with taking ecological considerations into account when developing new products. For example, the new *sleep•safe*™ cycler for peritoneal dialysis was designed to be used exclusively with entirely PVC-free disposables and also has a reduced plastic content. Thus, biocompatibility is maximized while any potential negative impact on the environment is minimized. We are also working to ensure that our production processes reflect the same level of concern for the environment. For example, in St. Wendel, Germany, as a result of our efforts to standardize and convert to more environmentally-friendly material, 50 % of all disposables for continuous ambulatory peritoneal dialysis (CAPD) are now PVC-free.

In addition, by optimizing production technology, energy consumption was significantly reduced. For example, electricity consumption for the drying of peritoneal dialysis systems after sterilization was reduced by 390 megawatt hours per year, which corresponds to the average annual consumption of 110 German households. In the Schweinfurt plant, we have succeeded in further reducing by 28 % the number of hazardous substances used, such as oils and adhesives. Despite a 16 % increase in the number of dialysis machines produced, internal waste and energy costs were reduced by 8 %.

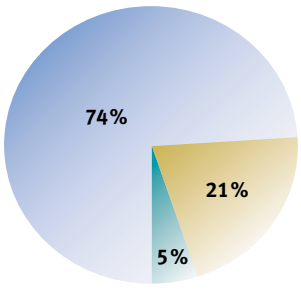
In 1999 we will continue our efforts to improve the environmental compatibility of our products and production processes. The corporate environmental management system will be certified and will initially be implemented in Germany in our manufacturing plants St. Wendel and Schweinfurt, as well as in R&D in Bad Homburg.

Employees

The number of full- and part-time employees totaled 28,739 worldwide on December 31, 1998 compared to 28,019 one year earlier. The decline in North America is primarily a result of the divestiture of the U.S. Homecare and Diagnostics businesses, which was partially offset by employees added due to acquisitions. The regional distribution of employees compared to the previous year remained basically unchanged.

74 % of the employees are in North America, 21 % in Europe and 5 % in other parts of the world. The number of employees in Germany as of December 1998 was 1,885.

Employees by Region



1998

North America
Europe
Rest of the world

Once again, the enthusiasm and hard work of our employees around the world were instrumental to our accomplishments in 1998. As in the previous year, non-managerial employees in Germany who have worked with the Company for at least three years will share in our success by receiving a portion of 1998 profits, which exceeds last years' amount of DM 1.050 by 15 %. The payment will be made mainly through preference shares. The participation for the 1997 fiscal year was paid out, mainly in preference shares, in 1998. Approximately 50 % of eligible employees also took advantage of the opportunity to invest in the Company's future by acquiring additional shares with their own funds.

A performance-based compensation plan is also in place for managerial employees; the variable component of the plan can increase base compensation by up to 40 %. In 1998, Fresenius Medical Care was one of the first companies in Germany to implement a stock option program for managers outside the U.S, which was approved at the annual shareholders' meeting.

In North America we continued to invest in our Business Practices and Compliance Program which is intended to promote high ethical standards and legal compliance throughout the organization. Training has been completed company-wide and will be provided on an ongoing basis for the over 21,000 employees in North America.

Employees by Region

	1998	1997	Change
North America	21,256	21,583	-2 %
Europe	6,016	5,348	12 %
Rest of the world	1,467	1,088	35 %
Total	**28,739**	**28,019**	**3 %**

Course of Business since January 1999

Since the close of 1998, there have been no major changes in the economic or business climate in which the Company operates. Our growth continues to be supported by favorable trends including overall growth in the number of patients requiring dialysis treatment as well as the ongoing consolidation in our industry.

Regarding the ongoing investigation in the U.S., there is no expectation as to the timing of a possible global resolution nor can the financial impact be reasonably estimated at the time of printing this report.

The financial turmoil in Brazil starting in January, which resulted in a sharp devaluation of the local currency, has not had a material effect on our overall business.

The development of business to date is in line with our expectations.

Nurse with hemodialysis machine

Outlook

Steadily Growing Markets

Fresenius Medical Care operates in a market that is characterized by relatively consistent growth. Worldwide, the dialysis patient population has been growing in the range of 7-9% per annum, a trend that is expected to continue in the future. An increase in general life-expectancy, enhanced treatment methods and a rise in the incidence of the illnesses which can lead to chronic kidney failure, such as diabetes and hypertension, for which no remedy is available, contribute to the favorable market outlook. Furthermore, transplantation, which is the only alternative to dialysis treatment, has only been possible for approximately 5% of all patients. Due to a shortage of donor organs this percentage has not increased in the past several years. Demand for healthcare in emerging markets is also expected to continue to grow as these national economies develop, allowing an increasing number of patients to gain access to life-saving dialysis treatment. In our primary markets in the industrialized world, we expect to see a continuation of cost-cutting measures in the healthcare sector. Ours is a highly regulated business and we cannot exclude regulatory changes in the future. As we have done in the past, we will respond to these challenges by developing alternative strategies and innovative products, improving therapeutic quality, and increasing overall productivity.

We believe that the consolidation among providers of dialysis care will continue, following the trend in the U.S. market where already over 60% of patients are currently treated by chain providers. Demand for high-quality treatment, strict cost management and the increased acceptance of private providers support the case for consolidation. Particularly in Western Europe, the shift towards private providers has already begun and will benefit chain providers such as Fresenius Medical Care as the pace of change intensifies. Our experience in providing care for over 74,200 patients worldwide, coupled with our long history of supplying dialysis products in over 100 countries of the world, provides us with a knowledge of local markets that will serve us well in this dynamic market. Accordingly, we expect the percentage of revenue attributable to Dialysis Care in the International segment to continue to increase. The expected growth in treatments along with our commitment to continuous product innovation should enable us to further increase our leading share of the global products business.

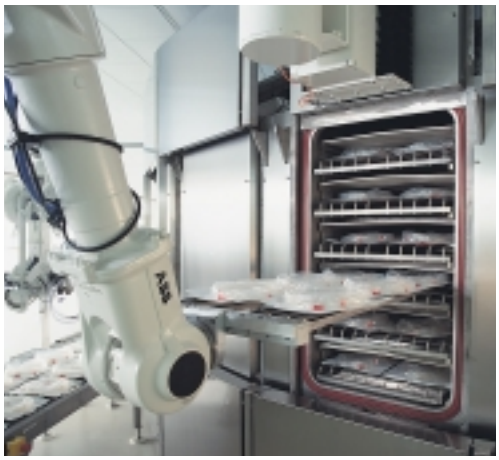
Staff of a
U.S. dialysis clinic

Changes in the German Market Environment
By implementing SAP/R3 software in conjunction with a special SAP euro update, the necessary technical and legal requirements of the conversion to the euro were met. By having these systems in place, Fresenius Medical Care was prepared to handle invoicing as well as payables in either euros or in any other currency as of January 1, 1999. We do not expect the introduction of the euro to have a significant impact on our business, nor do we expect any significant changes in our pricing or cost structure.

The positive and negative effects on our business of the planned tax reform based on the governmental projects that are known to date will most likely offset each other, so that no significant negative impact is presently expected.

Expected Revenue and Earnings Growth
Our past acquisitions of dialysis clinics, and certain, positive changes in U.S. reimbursement regulations, should continue to have a favorable effect on the Company's performance. Assuming stable foreign exchange rates, the absence of severe financial crises and no further legislative changes, we anticipate 10 % internal revenue growth in 1999. Planned product launches are also expected to contribute to this anticipated growth.

Assuming no major changes in factors impacting earnings, we expect earnings growth to exceed revenue growth in 1999 due to increased efficiencies in our base business, the integration of newly acquired clinics as well as lower interest costs. In 1999 these factors should lead to an increase in earnings per share of more than 25 % compared to the previous year.



In-line steam sterilization of bloodlines

“The difference between good care and superior care is often a smile, a kind word or a reassuring hug.”

Pei Yang, nurse, with patient in a Boston dialysis clinic

Thinking Ahead in Dialysis

During 1998 we continued to set new standards in the renal community in North America by providing quality patient care and innovative new products. We strengthened our leadership position by adding 67 clinics to our network, bringing the total to 782 clinics at year end 1998. We also expanded our product manufacturing plants, particularly our plant in Ogden, Utah, to meet the growing market demand for our biocompatible Fresenius Polysulfone® dialyzer, and our concentrate production facilities in California and New Jersey. The successful divestiture of our Homecare and Diagnostics businesses in mid-1998 enabled us to focus exclusively on our core Dialysis Products and Dialysis Care businesses which, in turn, also strengthened our financial performance.

Revenue in North America totaled $2.6 billion in 1998. Dialysis Care contributed 82% of total revenue and grew by a strong 22% compared to 1997. Dialysis Products revenue totaled $449 million, an increase of 7% over the previous year. EBITDA increased by 20% to $549 million and clearly benefited from the sale of non-core assets.

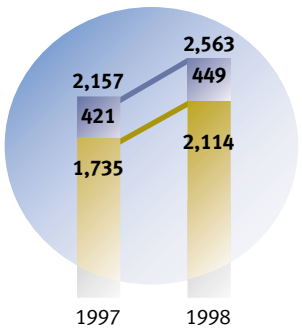
Dialysis Care

Our Dialysis Care operation is all about providing the very best in patient care and improving the life of our patients through personal attention and advances in therapy and technology. Our highly qualified nurses, dieticians, technicians, administrative staff and social workers, work hand-in-hand as a team with our physicians and medical directors, each contributing to our success. Fresenius Medical Care North America now treats 24% of all dialysis patients in the U.S. in a network of clinics that spans the continent and provided 8.2 million dialysis treatments during 1998. Our success is not measured by numbers alone, but also by the lives we help to save each day. In both regards, Fresenius Medical Care is the clear leader in dialysis care in North America.
To continue to build on this leadership base, Fresenius Medical Care North America is advancing its efforts in disease state management, an area of renal healthcare that is the focus of increased attention.

Initiatives underway include partnerships with some of the leading health organizations and providers in the nation including:

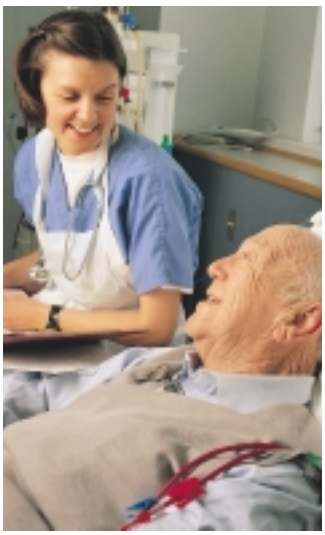
- Optimal Renal Care: A joint venture with Kaiser Health Plan's Southern California Permanente Medical Group;
- Renaissance Health Care: A joint venture with leading nephrologists from across the country;
- Renal Research Institute (RRI): A partnership with Beth Israel Medical Center in New York.

Revenue North America
$ in millions



	1998
Dialysis Care	+7%
Dialysis Products	+22%
Total	**+19%**

Segment Report: North America



Hemodialysis treatment in a U.S. clinic

Together, these efforts allow us to continuously improve the quality of care while, at the same time, helping us to control the total costs of treating the disease. To meet the changing needs of the market and to prepare for the transition from traditional fee-for-service reimbursement to fully capitated risk-sharing arrangements, we must continually strive for improvements in the quality of care as well as costs.

Another important element of our Dialysis Care business is the extensive patient database we maintain: the Patient Statistical Profile (PSP). It has a wealth of clinical information that is invaluable to our efforts in disease state management. Fresenius Medical Care has been collecting and analyzing information on its dialysis patients in the PSP since 1985. This data has enabled us to analyze patient outcomes, indicated by death and hospitalization rates, as well as to prepare comprehensive demographic and clinical information. These biostatistical analyses and research studies help us to understand how patient demographics and treatment affect outcomes. The insights gained from ongoing review of this clinical information are crucial to our effort to improve the quality of patient care.

Information obtained from our research enables Fresenius Medical Care's clinicians to formulate pertinent questions about patient care and outcomes that lead to reductions in dialysis patient mortality. These rigorous scientific and statistical analyses form the basis for new and better treatment therapies.

Optimal Renal Care, our joint venture with a division of the largest HMO in the U.S., is dedicated to managing end-stage renal disease (ESRD) with the aim of making the healthcare system more effective for the patient while reducing the overall cost associated with treating dialysis patients. Our joint venture partner Kaiser Permanente complements Fresenius Medical Care's expertise in providing highest quality care to dialysis patients with its clinical experience.

Renaissance Health Care, Inc. is a specialty managed care company dedicated to improving hemodialysis patient care through the development and operation of outpatient vascular access treatment and diagnostic facilities staffed by leading nephrologists or radiologists. Vascular access represents an enormous problem for dialysis patients and, because of the frequent need for hospitalization, is a costly burden for the healthcare system. In the U.S. more than $1 billion is spent annually on this aspect of care alone. We intend to establish vascular access centers across the country over the next three years in order to treat patients in a more cost-effective manner by better managing this critical aspect of care.

The Renal Research Institute was formed in 1997 to find new and better methods of improving the quality of life and outcomes for dialysis patients. To meet this goal, the RRI is performing research and developing new technologies in state-of-the art dialysis clinics. The broad spectrum of issues under scrutiny include hemodialysis, peritoneal dialysis, and the pre-ESRD population. Theoretical and mathematical research (e.g. urea kinetic modeling) will play a key role in the RRI's studies. In addition, new dialysis technology and treatment methods will be continuously developed and evaluated.

Laboratory Services

Laboratory services are a vital part of the dialysis treatment that Fresenius Medical Care North America provides. During 1998, our laboratory service business, Spectra Renal Management, continued its pattern of growth by performing nearly 37 million tests. This enabled the Company to capture a leading market share of approximately 36 % for dialysis patients in the U.S. Our three laboratory sites, in Fremont and Woodland Hills, California, and Rockleigh, New Jersey, provided services for 1,150 dialysis clinics in 50 states.

1998 also marked the release of enhancements to Spectra Renal Management's Lia® (Laboratory Information Access) laboratory reporting and outcome monitoring software. These software enhancements allow clients to display trends and to analyze and graph additional laboratory results. In 1999, we plan to adopt a universal remote order entry system for our customers that will provide added convenience and accuracy.

In addition to laboratory services, Spectra Renal Management provides mobile diagnostic services for ESRD patients, including echocardiography, doppler flow testing and nerve conduction studies. In 1999, Spectra Renal Management will launch Best Medical Practices for vascular management to improve early detection of vascular issues.

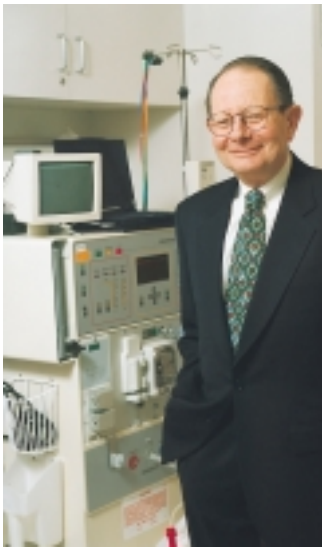
Dialysis Products

1998 was a year of major accomplishments for the Dialysis Products business. In hemodialysis, we began 1998 by announcing a new approach to continuous slow flow dialysis for critically-ill patients with acute renal failure in an intensive care unit setting. Instead of using expensive, dedicated devices and sterile solutions, a standard Fresenius 2008H dialysis system provides a cost-efficient and improved treatment with a bicarbonate buffered solution and enhanced clearance.

We are also developing the next generation of dialysis machine technology, the 2008K, for the North American market. This series will offer new touch screen treatment navigation and on-screen trending in addition to Online Clearance, Blood Temperature Monitor™ and Blood Volume Monitor™. The Online Clearance Monitor is also available as an integrated module for the 2008H series of hemodialysis machines. The 2008K generation will also introduce a system with an integrated ultrapure dialysate filter called DIASAFE®.

We also successfully introduced a line of non-reuse dialyzers that expands our line of biocompatible Fresenius Polysulfone® dialyzers with a higher performance dialyzer. The F70NR, F7NR, F50NR and F5NR dialyzers targeted for the non-reuse market segment are both high-flux and high-efficiency membranes. Our year-end 1998 market share in the U.S. for Fresenius Polysulfone® dialyzers was about 50 %.

Our peritoneal dialysis products group increased its market position in automated peritoneal dialysis by growing at a rate of approximately 15 % compared to the industry growth rate of about 10 %. We also introduced the IQcard™ which is used with the Freedom™ PD-PLUS cycler to monitor patient compliance while dialyzing at home.



Nathan Levin, M.D.
Medical Research Director
Renal Research Institute

“It is people’s dedication in caring for other people that guides technological advances and determines the quality of dialysis.”

Guy Laurent, M.D.
European Medical Advisory Board
Centre de Rein Artificiel, Tassin, France

Seizing Opportunities in Global Markets

With a revenue of $ 943 million, an increase of 15 %, or 19 % if exchange rate effects are eliminated, and further improvement in the EBITDA margin which rose by 70 basis points, 1998 marked another year of successful performance. High growth rates in all regions and a strong performance in Dialysis Products with above-market growth rates contributed to this achievement. Revenue in our Dialysis Care business rose by 48 %, indicating further penetration of international markets. Our aim has been to use our successful products business in over 100 countries as a platform for growth in Dialysis Care and, we are pleased to report, much progress has been made. At the end of 1998, 22 % of total treatments were provided internationally, a reflection of our efforts to vertically integrate the products and services businesses as well as overall growth in the various markets.

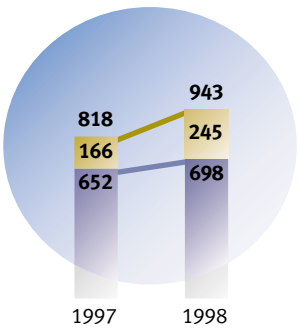
Europe, Middle East, Africa

In 1998 the product business remained the dominant part of Fresenius Medical Care's operations in Central Europe. Altogether, Fresenius Medical Care was able to maintain its clear, overall market leadership through continued volume growth. In addition, our market share in the Netherlands, Belgium and Switzerland increased compared to the previous year. The introduction of the advanced hemodialysis ONLINE *plus*™ system together with the successful expansion of the dialyzer program, when the HDF100S and F10HPS were launched in the second half of 1998, had a positive impact on the overall hemodialysis business. In peritoneal dialysis, the CAPD *stay•safe*® system gained market share in a highly competitive environment. Volume growth and increased efficiencies as a result of the integration of the Benelux countries (formerly included in the Northern European region, which was dissolved effective January 1, 1998) offset continued pricing pressure.

The total market for dialysis products in Central Europe increased by approximately 4 % in 1998, and it is expected that this trend will continue in 1999. Based on our excellent market position and the widespread introduction of the new *sleep•safe*™ peritoneal dialysis cycler planned for 1999, we are confident that we can achieve further market penetration in Central Europe.

In Western Europe we continued to expand our market position with a revenue increase of 22 % in 1998. This is primarily due to the acquisition of dialysis clinics in Italy, France and Spain. Dialysis Care represents a large share of total revenue in this region, with Spain and Portugal as the major contributors. Acquisitions in Catalonia complemented our nationwide network of dialysis clinics in Spain. In 1998, Fresenius Medical Care also acquired dialysis clinics in Italy and France for the first time. During 1998, we continued the implementation of ISO 9002 quality certification and achieved certification in 14 Spanish, three British and two Portuguese clinics by the end of the year. Fresenius Medical Care is the first dialysis company to implement quality management systems in dialysis clinics with certification determined by independent notified bodies. In Portugal, Fresenius Medical Care stopped the practice of dialyzer reuse in its own clinics and started a phase-out program in the United Kingdom in combination with the certification for ISO 9002. We intend to expand the certification program to a growing number of clinics in 1999.

Revenue International
$ in millions



	1998
Dialysis Care	+ 48 %
Dialysis Products	+ 7 %
Total	**+ 15 %**

Segment Report: International

The European Scientific Council, established during 1998, allows Fresenius Medical Care and its medical doctors to collaborate closely with key European nephrologists on topics relevant to the development of best medical practices in dialysis. In 1998, the Clinical Management team began implementing guidelines and recommendations. It collected individual patient data and worked to enhance the scientific relationship with our nephrologists, in addition to expanding educational programs for doctors and nurses.

As in Central Europe, 1998 marked the launch of new dialysis machines equipped with ONLINE*plus*™ for hemodiafiltration, the biBag® dry bicarbonate concentrate as well as the latest innovations in dialyzers in Western European markets with a focus on Spain, Italy and France.

In Northern and Eastern Europe, the Russian economic crisis had a slightly negative impact on our business, especially during the second half of the year. While revenue growth for the year as a whole was a respectable 15 %, we expect the lingering effects of Russia's financial woes to slow down growth in the region over the next few years. In the interim, we will proceed cautiously with regard to new investment as we continue to believe in the Russian market's long-term potential.

Other Eastern European markets remained stable, allowing us to achieve good revenue growth. We expect similar growth rates in 1999 given that funds dedicated to healthcare are steadily increasing. Our focus in 1999 will be on Romania, Slovakia, Slovenia, the Baltic countries and Poland.

Focusing on countries without production facilities for liquid concentrates, we successfully introduced our Granudial® and biBag® dry concentrates. The *stay•safe*® peritoneal dialysis system is being well received in the region. The Company's AQUASAFE 08™ water treatment plant was installed in a growing number of our own clinics and in external facilities.

Dialysis Care still plays a minor role in Eastern Europe. However, Fresenius Medical Care operates dialysis clinics in Hungary and the Czech Republic. Due to public budget restrictions, growth was limited in Hungary. However, privatization will most likely create new opportunities to enter Dialysis Care in countries like Slovakia and Poland in the relatively near future.

As in previous years, our market share in the Middle East and in Africa again increased. Dialyzer sales, which doubled compared to 1997, made a significant contribution. Our joint venture MDC in Saudi Arabia achieved CE certification for its dialyzers, a major step forward for our business in the Middle East.

Staff of dialysis clinic in Asia

Production for liquid concentrates in Turkey was further expanded. Turkey is the only country of this region where we operate dialysis clinics. In 1998, we formed a joint venture with the National Kidney Foundation and operated three clinics at the end of 1998.

Asia-Pacific

Despite the significant devaluation of some major Asian currencies as a consequence of the region's financial crisis, revenue in this region grew 12 % as reported in U.S. dollars and 26 % when adjusted for exchange rates.

Our key markets – including Japan, South Korea, Taiwan, Hong Kong and Australia, which are among the more developed economies of the area Asia-Pacific – witnessed stronger demand for our products and services, albeit with increased pricing pressure. In mainland China we saw a similar trend with a significant revenue increase in local currency. Our business in the emerging markets in South-East Asia was affected by the region's economic turmoil. This caused significant reductions in public spending on medical equipment in Indonesia, Thailand and, to a lesser extent, in Malaysia.

During 1998, we reorganized our business in Asia-Pacific by creating the regions Japan, Greater China, Central Asia and South Asia Pacific with regional headquarters in Hong Kong in order to address the local markets more effectively.

In Japan, the most significant market in the region, Fresenius Medical Care increased its ownership in Fresenius Kawasumi from 50 % to 70 %. Fresenius Kawasumi will continue to produce fibers for Fresenius Polysulfone® dialyzers, but the new co-marketing arrangement allows Fresenius Medical Care to market dialyzers independently from Kawasumi Laboratories in Japan. As a result, dialyzer sales are expected to grow at an increased rate in the future.

Dialyzers contributed significantly to the overall growth achieved in Asia-Pacific, with the greatest increase in Australia where dialyzer sales grew by more than 200 %. Sales of hemodialysis machines were strong, especially in South Korea and Australia. The *stay•safe*® peritoneal dialysis system continued to gain acceptance in South Korea and Hong Kong, where we have achieved a 30 % market share since the product's launch in 1997. In Taiwan, our second largest market in the region, we introduced peritoneal dialysis products to complement our hemodialysis product line.

At year end, a total of 19 clinics in Asia-Pacific were part of our global network. Going forward, we intend to further capitalize on opportunities for growth in Dialysis Care with particular emphasis on Taiwan, South Korea and Australia.

Latin America

The positive, double-digit revenue growth of the previous year continued in 1998 with revenue growth of 30 %. Our performance during the year was only slightly impacted by the economic crisis in Latin America as the situation in Argentina, our largest market in the region, remained relatively stable. In other countries, currency fluctuations and increased financing costs affected results to some extent.

The Dialysis Care business was the main growth driver in Latin America. In a total of 88 clinics, 6,400 patients were treated. The particularly good growth rates achieved in Argentina and Colombia enabled us to further expand our leading market position in these markets. To facilitate more efficient operation in the future, the Dialysis Products and Dialysis Care businesses in Argentina and Colombia were combined into a single organizational unit in both countries. The healthcare systems in both countries are fairly well developed and we are now able to offer country-wide networks to HMOs. New clinic openings helped to drive growth in Venezuela. We signed an agreement with Petroleum de Venezuela (PDVSA), the national petroleum company, which provides for the treatment of dialysis patients covered by the PDVSA private insurance program.

Our manufacturing plant in Brazil increased its capacity to produce the A.N.D.Y. *PLUS*® peritoneal dialysis system in order to meet the still growing demand in the region.

Also in 1998, the regional headquarters for Latin America was moved to Miami, Florida, in order to more effectively manage the Latin American business.

Hemodialysis treatment in a Colombian dialysis clinic

“When in Africa, I become aware of the importance of our products and work in the region, as they enable patients to gain access to life-saving treatment.”

Yasmin Rachid
Sales Manager Africa

The Continuum of Care

'Setting superior standards in renal patient care' means that Fresenius Medical Care is dedicated to improving the quality of life of dialysis patients by continuously striving for better treatment outcomes. This ambitious aim cannot be reduced to a single therapy parameter or to an individual technical component. Rather, our leadership in renal care is the result of our systemic approach, which encompasses all aspects that determine the nature and quality of treatment.

This focus on the full continuum of care is reflected in our concept of BioAdequacy™, or individualized patient care in the most biocompatible way, which comprises both dialysis products and dialysis-related services. In addition, this systemic approach enables us to offer fully-integrated solutions that take into consideration resource constraints as well as the special needs of patients, medical professionals, insurers and regulatory bodies. This unique approach is also reflected in our product development. For example, the *sleep•safe*™ system combines material properties and device characteristics with the overall goal of improving outcomes.

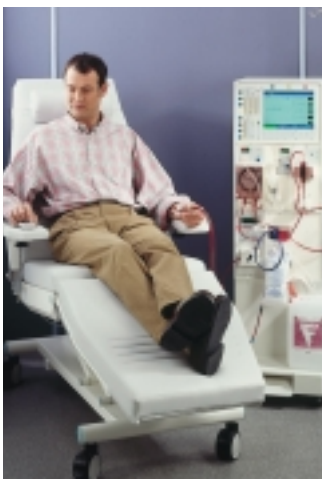
With a long history of success in dialysis products, Fresenius Medical Care was uniquely positioned to lead the consolidation in dialysis care, a process that began more than two years ago. Today, we are the global leader in the dialysis field and are in an even better position to accelerate the development and application of state-of-the-art product technology. Our network of dedicated caregivers and our research-based, scientific methods will continue to drive innovation, which should result in further improvement in patient outcomes, the ultimate measure of our success.

Offering a Choice of Technologically Leading Products

Fresenius Medical Care's comprehensive range of products includes products for both treatment alternatives – hemodialysis and peritoneal dialysis – which allows doctors and patients the freedom to choose the most efficacious treatment given a particular set of circumstances. Consistent, above-market growth rates in our Dialysis Product business reflect the value that the market places on our high-quality products.

Our R&D team strives to maintain the technological edge. Some examples of our commitment to technological leadership are: The unique, actively closed-loop control technology in blood volume measurement with the Blood Volume Monitor™, cost-efficient dose assessment techniques with Online Clearance measurement, and vascular access monitoring as well as recirculation measurement with the Blood Temperature Monitor™.

Our successful product business has also been the basis for expanding into dialysis care in selected countries and has proven to be a major benefit. Not only are nephrologists familiar with the quality of Fresenius Medical Care's products, but also joint venture partners or doctors who wish to cooperate more closely with Fresenius Medical Care can be assured that their patients will receive high-quality care and access to leading products.

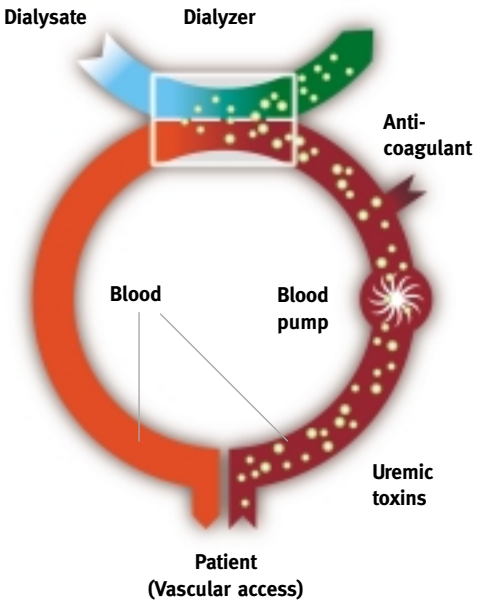


Hemodialysis treatment

Special Topic: Vertical Integration

Our hemodialysis machines have traditionally been characterized by their unique, modular structure which enables patient care providers to define the machine that exactly corresponds to the given patient's special needs. Newly-developed modules can, in most cases, be used to upgrade existing machines. Again, the choice will depend on the individual patient's needs.

All of our hemodialysis machines are based on the volumetric ultrafiltration control system and its reliability has led our machines to become the world's top-selling hemodialysis machines. Economies of scale in the production process are a logical consequence of our leading market position.



Principle of Hemodialysis

In hemodialysis the blood flows outside of the patient's body through disposable bloodlines into a specially designed filter, the dialyzer. The dialyzer assumes, more or less, the function of an artificial kidney by separating waste products and excess water from the blood. Dialysis solution carries away waste products and excess water and the cleansed blood is returned to the patient. The process is controlled by a hemodialysis machine, which pumps blood, adds anticoagulants, regulates the purification process and controls the mixing of the dialysis solution and its flow rate through the system. A patient typically receives three treatments per week, lasting from three to six hours each.

Enhancing Dialysis Therapy

In a network of 1,000 clinics worldwide more than 20,000 employees in Dialysis Care are dedicated to providing the best medical treatment for our patients, who can rely on the quality of Fresenius Medical Care's products and the availability of the latest technology. In turn, our clinics collect individual patient data that show the interaction of different important parameters over time. This data is necessary to develop new therapies and provides our R&D staff with critical information that helps to direct their activities. The analysis of clinical data through our Patient Statistical Profile database in the U.S., which has recently been augmented with a second generation data warehouse, constitutes one of Fresenius Medical Care's proven strengths. This database is the most comprehensive of its kind and enables doctors to see how clinics compare to the Company average, a regional average or the overall national average. In addition, we offer innovative renal laboratory and diagnostics services that go beyond simple dialysis treatment and are suited to complete patient care.

In North America, the Renal Research Institute, a joint venture between Fresenius Medical Care and Beth Israel Medical Center, combines a comprehensive research program with delivery of the highest quality clinical care to renal patients. Its commitment to a high level of scientific and methodological rigor, combined with strong ties to academic research institutions, makes it unique in the renal industry. Its complement in Europe is the European Scientific Council.

Our commitment to ensuring overall quality is also evident in the ISO certification program that was initiated in 1998. This is unique in the field of dialysis clinics and is evidence of the high standards that we have set for ourselves.

Developing New Concepts for Dialysis

For several years, payors in the U.S. have focused on reducing cost in healthcare. More recently, the total cost of treating a dialysis patient has been the subject of increased scrutiny. As a result, providers like Fresenius Medical Care are faced with the challenge of containing the overall cost of treatment without sacrificing patient well-being. Disease state management, which allows for the full continuum of patient care, replaces traditional fee-for-service reimbursement with fully capitated risk-sharing arrangements. Fresenius Medical Care is at the forefront of this emerging trend with over 800 patients enrolled in disease state management projects that will run for several years.

Again, we are taking a systemic, multi-disciplinary approach to meet this complex challenge. Capitated reimbursement, combined with the assumption of either partial or full risk of hospitalization cost, is negligible today, but will account for an estimated 25 % of dialysis patients treated in the U.S. in the year 2002. The success of disease state management is directly linked to the ability to cut hospitalization costs, which account for roughly 33 % of the overall cost of treating a dialysis patient. Fresenius Medical Care is well positioned to benefit from this trend through its joint ventures Optimal Renal Care and Renaissance Health Care. Optimal Renal Care provides all dialysis services under a single capitation rate, i.e. a flat fee per patient per month. Our combined experience offers the ability to predict with greater certainty the costs associated with providing care for a dialysis patient. Renaissance Health Care not only offers disease management, but also additional dialysis-related services like vascular access management. Problems with vascular access are the number one reason for hospitalization among hemodialysis patients in the U.S. In both joint ventures, capitation savings are shared between the partners, which creates a clear incentive for all parties involved.

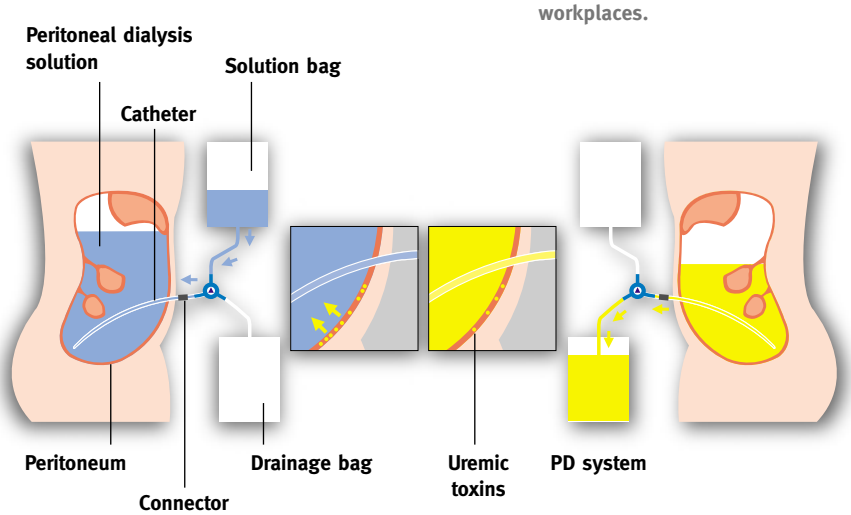
High-quality care combined with superior products convincingly addresses medical and economic issues in dialysis. Although our ONLINE *plus*™ therapy and products such as our high-flux dialyzers initially appear to be more costly, they improve clinical outcomes and lower total patient cost by reducing the need for expensive hospitalization.

Outside the U.S., particularly in Western Europe, we believe the trend towards increased cost awareness will lead to a further focus on private providers as a viable alternative. Fresenius Medical Care, which is recognized as the number one private provider of dialysis care through its network of 111 clinics in Europe, is well positioned to take advantage of the significant opportunities presented by this evolving market.

Our continuous effort to provide the highest quality care, combined with our position as the clear world leader in dialysis, provides a strategic advantage that will enable us to face the challenges of the future as well as to actively promote market changes.

Principle of Peritoneal Dialysis

Peritoneal dialysis removes waste products from the blood by use of the peritoneum, the membrane covering the intestinal organs located in the abdominal cavity. Using a surgically implanted catheter, a sterile dialysis solution is introduced into, and removed from, the peritoneal cavity several times a day. The peritoneum operates as the dialyzing membrane. Most peritoneal dialysis treatments are self-administered by patients in their homes or workplaces.



“It’s the dynamic, innovative working environment that first impressed us here and where we see good potential for our future careers.”

Robert Craig, Michael Meißner and Nino Riegel
Apprentices in the Schweinfurt plant, Germany

Management's Discussion and Analysis

Contents

Blaupausen nur bis Seite 34 !!!!

The Company

Fresenius Medical Care AG ("Fresenius Medical Care", "the Company" or "FMC") was formed on September 30, 1996 through the merger (the "Merger") of the global dialysis businesses of Fresenius AG and W.R. Grace & Co. ("W.R. Grace"). The Company was organized in a series of transtively. Effective October 1, 1996, FNMC acquired 100 % of FUSA from the Company.
Additionally, in conjunction with the Merger, each holder of W.R. Grace common stock received one share of a Class D Preferred stock of FNMC for each share of W.R. Grace common stock previously held. The Class D preferred stock entitles the holder to receive, when, and if and as declared by the board of directors of FNMC, a special dividend, payable in cash in annual installments beginning on October, 2002 (and in each subsequent year until the dividend is fully paid) in an amount based on the adjusted cash flow, as defined in the terms of the Class D Preferred Stock, of Fresenius Medical Care AG for the period from January 1, 1997 to December 31, 2001.
On June 12, 1997 FNMC, by vote of its shareholders, changed its name to Fresenius Medical Care Holdings, Inc. ("FMCH").

Shared Production and Services

Prior to the consummation of the Merger, FMC shared certain manufacturing facilities with Fresenius AG's other businesses. In connection with the Merger, in each situation where facilities were shared, post-Merger ownership of the location or manufacturing facility (collectively, the allocated to FMC at fully absorbed cost.
Fresenius Medical Care and Fresenius AG have entered into supply agreements for the purchase and sale of products from the Retained Facilities and the Transferred Facilities.
As a division of Fresenius AG, FMC obtained administrative and other services from Fresenius AG headquarters and from other divisions and subsidiaries of Fresenius AG. Conversely, FMC provided certain services to other divisions and subsidiaries of Fresenius AG. Fresenius Medical Care and Fresenius AG have entered into transitional agreements for continuation of many of such services.

Real Estate Located in Germany

Certain land, manufacturing and office buildings located in Germany have been retained by Fresenius AG and leased by Fresenius AG (or an affiliate) to Fresenius Medical Care (or an affiliate) under operating lease agreements. Accordingly, such land and buildings have been excluded from the consolidated balance sheets. The consolidated statements of earnings included elsewhere herein include, for the year ended December 31, 1996, $1.2 million of depreciation expense related to such facilities representing an assumed charge to FMC from Fresenius AG for the use of the land and buildings. Under such leases, Fresenius Medical Care has agreed to pay Fresenius AG DM 16.8 million per year, escalating annually beginning in 1998, based upon the German cost of living index for a four-person employee household, representing a fair market rental value for such properties. The leases for manufacturing facilities have a term of 10 years with options to renew. The leases for other facilities have a term of 10 years.

Financial Condition and Results of Operations

The following is a discussion of the financial condition and results of operations of FMC. The discussion should be read in conjunction with the consolidated financial statements included elsewhere in this document. The disaggregated financial results for FMC set forth in the table below entitled "Fresenius Medical Care AG Segment Data" have been prepared using a management approach, consistent with the basis and manner in which FMC management internally disaggregates financial information for the purposes of assisting in making internal operating decisions and evaluating management performance.

This section contains certain forward-looking statements. These forward-looking statements are made based on management's expectations and beliefs concerning future events which may affect FMC, but no assurance can be given that such events will occur or that the results will be as anticipated.

Overview

Effective January 1, 1998, FMC adopted SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*, for its year-end reporting requirements. The Company identified two reportable operating segments, North America and International, that were determined based upon how the company manages its businesses. Both segments are primarily engaged in a) providing kidney dialysis services and performing related clinical laboratory testing and renal diagnostic services and b) manufacturing and distributing products and equipment for the treatment of end-stage renal disease. The management of each operating segment is under the supervision of the Managing Board Members responsible for the profitability and cash flow of each segment's various businesses. The accounting policies of the operating segments are the same as those applied in preparing the Company's consolidated financial statements under U.S. GAAP.

Management evaluates the segments using a measure that reflects all of the segment's controllable revenue and expenses. The most appropriate measure in this regard is earnings before interest and taxes ("EBIT") which Management believes measures the Company's source of earnings. As financing is a corporate function, it is not under the control of the segments and therefore interest cost is not included as a segment measurement. Taxes are also regarded to be outside the segment's control. In addition to EBIT, management believes that earnings before interest, taxes, depreciation and amortization ("EBITDA") is helpful for investors as a measurement of the segment's and the Company's ability to generate cash and to service its financing obligations. EBITDA is also the basis for determining the compliance with certain covenants contained in the NMC Credit Agreement and the indentures relating to the Trust Preferred Securities.

EBITDA should not be construed as an alternative to net earnings determined in accordance with generally accepted accounting principles or to cash flow from operations, investing activities or financing activities or as a measure of cash flows. The Company believes its EBIT calculation is the functional equivalent of operating income. Because EBITDA and EBIT are not calculated consistently by all companies, the presentation herein may not be comparable to other similarly titled measures of other companies.

During 1998, the Company had discontinued operations resulting from its divestiture of its Homecare and non-renal Diagnostics businesses. The Company's results of operations also reflect an accounting change relating to start-up costs as a result of early adoption of Statement of Position No. 98-5, *Reporting on the Costs of Start-up Activities* ("SOP 98-5") as issued by the Accounting Standards Executive Committee ("AcSEC") of the American Institute of Certified Public Accountants ("AICPA"). Discontinued operations have been separately identified for each year included for analysis, while the cumulative effect of the accounting change are only shown for 1998.

The Company derives a significant portion of its global Dialysis Care net revenue from government health care programs (approximately 50 % in 1998). The reimbursement rates under these programs, including the Composite Rate, the reimbursement rate for EPO (which accounted for approximately 26 % of North America's Dialysis Care revenue in 1998), and the reimbursement rates for other dialysis and non-dialysis related services and products, as well as other material aspects of these programs, have in the past and may in the future be changed as a result of deficit reduction and health care reform measures.

The Company's business, financial position and results of operations also could be materially adversely affected by an adverse outcome in the OIG investigations, any whistleblower action, the pending challenge by the Company to changes effected by Medicare in approving reimbursement claims relating to the administration of IDPN or the adoption in 1996 of a new coverage policy that has changed IDPN coverage prospectively. The Company's business, financial position and results of operations would also be materially affected by an adverse outcome in the pending litigation concerning the implementation of certain provisions of OBRA 93 relating to the coordination of benefits between Medicare and employer health plans in the case of certain dual eligible ESRD patients.

The Company also derives a significant portion of its net revenues from reimbursement by non-government payors. Historically, reimbursement rates paid by these payors generally have been higher than government program rates in their respective countries. However, non-government payors are imposing cost containment measures that are creating significant downward pressure on reimbursement levels that the Company receives for its services and products.

Results of Operations

The following table summarizes the financial performance and certain operating results and pro forma operating results of the Company by principal business segments for the periods indicated. Inter-segment sales primarily reflect sales of medical equipment and supplies from International to North America. This information has been reorganized and prior period information has been reclassified to conform with the business segment reporting requirements of FMC and to distinguish between continuing and discontinued operations and the cumulative effect of the accounting change as previously noted.

Segment Data

Year ended December 31	**1998**	**1997**	**1996** [1]
Total revenue			
North America	2,565	2,157	1,927
International	986	867	812
Totals	**3,551**	**3,024**	**2,739**
Inter-segment revenue			
North America	2	1	2
International	43	49	47
Totals	**45**	**50**	**49**
Total net revenue			
North America	2,563	2,156	1,925
International	943	818	765
Totals	**3,506**	**2,974**	**2,690**
EBITDA			
North America	549	457	358
International	228	192	178
Corporate	(9)	(8)	(7)
Totals	**768**	**641**	**529**
Amortization and depreciation			
North America	215	199	168
International	62	50	47
Corporate	2	1	0
Totals	**279**	**250**	**215**
Non-recurring charges International			**29**
EBIT			
North America	334	258	190
International	165	142	102
Corporate	(10)	(9)	(7)
Totals	**489**	**391**	**285**
Interest, net	(220)	(184)	(156)
Income tax expense	(135)	(101)	(81)
Minority interest	(2)	(2)	
Loss from discontinued operations, net	(106)	(14)	(4)
Cumulative effect of accounting change, net	(7)		
Net income	**19**	**90**	**44**

$ in millions
unaudited

1) pro forma

1998 Compared to 1997

Net revenue for 1998 increased by 18% (19% at constant exchange rates) to $3,506 million from 1997 levels. Income from continuing operations increased to $132 million, a 27% increase. Pre-tax earnings rose 30% to $269 million in 1998. After the effect of an accounting change of $7 million, losses from the operations of discontinued businesses of $9 million and the loss of disposal of those businesses, $97 million, all net of tax, minority interest, and income tax expense, net income for 1998 was $19 million.

The following discussions pertain to the Company's business segments and the measures the Company uses to manage these segments. These discussions are based on continuing operations unless otherwise indicated.

North America segment

Net revenue for the North America segment grew by 19% from $2,156 million to $2,563 in 1998 as a result of a 22% increase in Dialysis Care revenue to $2,114 million and a 7% increase in Dialysis products revenue to $449 million. Dialysis Care achieved a 14% growth in base business primarily as a result of increased treatments (6%), favorable treatment rate improvements (2%) and increased ancillary services (4%). Acquisitions contributed 7% of the total growth. Dialysis Product revenue grew by 7% due to increased sales of dialyzers, machines and concentrates, partially offset by decreased sales of bloodlines, peritoneal and other products.

EBITDA

EBITDA for the North American segment grew by 20% as a result of the increase in the base business, improved treatment rates, and increased ancillary services noted above and production efficiencies resulting from increased production. Acquisitions contributed 9%. Partially offsetting these improvements were corporate costs that were $37 million higher, primarily due to foreign exchange gains of $28 million recognized in 1997 and increased insurance and legal expense.

Amortization and depreciation

Amortization and depreciation decreased, as a percentage of revenue, to 8.4% in 1998 from 9.2% in 1997. This is mainly due to the impact of internal revenue growth while straight-line write-off of the goodwill associated with the Merger and prior years' acquisitions has remained fairly constant.

EBIT

EBIT for the North American segment increased by 30% as a result of the increase in EBITDA and the positive impact of the decreased rate of amortization and depreciation to revenue as previously mentioned.

International segment

Net revenue for the International segment grew by 15% (19% at constant exchange rates) from $818 million to $943 as a result of a 30% (39% at constant exchange rates) increase in the Latin American region, 12% (26% at constant exchange rates) growth in the Asia-Pacific region and a 14% (16% at exchange constant rates) increase in the European region. The Company's Latin American business was only slightly impacted by the economic crisis in that region as the situation in Argentina, FMC's largest market in the region, remained relatively stable. The currency fluctuations of the other countries in the Latin American region had a slight impact on operations. The crisis in the Asia-Pacific area had little impact on the Company's key markets which are among the more developed countries. The Company's business in the emerging markets of Indonesia, Thailand and, to a lesser extent, in Malaysia, in the Asian-Pacific region were affected by the economic turmoil which resulted in significant reductions in public spending on medical equipment in those emerging markets. Total Dialysis Care revenue increased by 48% (52% at constant rates) to $245 million. Base business Dialysis Care treatments increased by 6% resulting in a 2% revenue growth. Acquisitions accounted for 9% of the total revenue growth. Total Dialysis Product revenue increased by 7% (10% at constant exchange rates) to $698 million.

EBITDA

EBITDA for the International segment grew by 19% (21% at constant exchange rates) primarily as a result of the increase of revenue as noted above and a contribution from acquisitions of 6%.

Amortization and depreciation

Amortization and depreciation increased, as a percentage of revenue, to 6.6% in 1998 from 6.1% in 1997. This is mainly due to the impact of acquisitions made in 1997 and 1998, and the adjustments of carrying values for impaired assets ($2 million) in 1997.

EBIT

EBIT for the International segment grew 16% (19% at constant exchange rates) as a result of the increased EBITDA mentioned above, partially offset by a 24% increase in depreciation and amortization expense. Depreciation and amortization was higher due to higher capital spending in the current year over the prior year and the aforementioned adjustments of carrying values.

The following discussions pertain to total Company costs:

Interest

Interest expense for 1998 increased by 20% reflecting the impact of a full year's cost of borrowings used to finance the prior and current year's acquisitions and the cost of borrowing funds to redeem convertible equity securities.

Income taxes

The effective tax rate grew to 50.2% in 1998 from 48.9% for the same period in the prior year. This was primarily a result of the use of NOLs in 1997 and the reduction of dividend distribution credits available in 1998 as compared to 1997.

Liquidity and capital resources

Fresenius Medical Care generated cash from operating activities of $ 268 million in 1998 and $ 216 million in 1997. Cash on hand was $ 32 million and $ 38 million, at year end 1998 and 1997, respectively.

The Company made acquisitions of $ 265 million and $ 527 million in 1998 and 1997, respectively. In addition, capital expenditures for property, plant and equipment were made in the amount of $ 159 million and $ 209 million in 1998, and 1997, respectively. Acquisitions and capital expenditures were made in the North American segment in the amount of $ 245 million and $ 607 million for the years 1998 and 1997, respectively. International segment capital spending was $ 178 million and $ 125 million, respectively, for 1998, and 1997. The capital expenditures were used for automation of production processes and increased production capacity, internal expansion, improvements, furnishings and equipment.

In February 1998, the Company issued $ 450 million of 7 $^{7}/_{8}$% USD Trust Preferred Securities and DM 300 million 7 $^{3}/_{8}$% DM Trust Preferred Securities for net proceeds of approximately $ 600 million. The voting securities of the issuers of the securities are 100 % owned by FMC and have as their sole assets senior subordinated debentures due 2008, issued by a subsidiary, and related guarantees by the Company and certain subsidiaries. The proceeds were used to permanently pay down $ 250 million on Facility 2 of the NMC Credit Agreement thereby reducing the total credit facility to $ 1.75 billion, which is in the form of a $ 750 million term loan (Facility 2) and a $ 1 billion revolving loan (Facility 1). The remaining $ 350 million was used to reduce other debt and for other general corporate purposes. Although the Company did not reduce its total debt as a result of this Trust Preferred financing, it did increase its flexibility within its primary credit agreement to access additional funds.

Total long-term debt at year-end 1998 decreased to $ 1,127 million from $ 1,658 million as a result of the Trust Preferred Securities transaction noted above. Short-term debt increased slightly in 1998 to $ 169 million from the 1997 level of $ 153 million. During the year ended December 31, 1998, the Company satisfied its obligation relating to the equity securities issued by FMC Finance, S.A., in conjunction with acquisitions made in 1997 and early 1998. A total of approximately $ 62 million nominal amount of these securities was retired and approximately $ 6 million nominal amount of these securities remain outstanding and was reclassified as a liability at year end 1998.

In February 1998, the Company's receivables financing facility entered into on August 28, 1997, was increased to $ 331 million from $ 204 million. The current agreement has an effective interest rate of 5.30 % and matures on September 27, 1999. Proceeds of $ 306 million have been drawn down under the agreement at year-end 1998 and $ 200 million had been drawn down at year-end 1997.

The Company has entered into interest rate swap agreements with various commercial banks for notional amounts totaling $ 1,450 million. These agreements effectively fix the Company's variable interest rate exposure on the majority of its revolving loans and accounts receivable securitization programs to fixed rates of interest between 6.05 % and 6.6 %. These swap agreements expire at various dates between January 2000 and January 2004. Under the NMC Credit Agreement, FMC has agreed to maintain at least $ 500 million of interest rate protection.

Under the NMC Credit Agreement, dividend payments by NMC to FMCH in any year may not exceed 50 % of NMC's consolidated income (as defined in the NMC Credit Agreement) for the preceding year. Such limitation does not apply to other first-tier subsidiaries of FMCH.

In 1998, the Company declared and paid dividends totaling approximately $ 45 million for fiscal year 1997 on its ordinary and preference shares. Included in the dividends were arrearages of approximately $ 1 million with respect to fiscal 1996. In addition, the Company paid $ 4 million of dividends to Fresenius AG relating to pre-Merger earnings that were not distributed at the time of the Merger. This distribution was delayed, by agreement, due to the application of local generally accepted accounting principles in determining the amount of pre-Merger earnings and the legal requirement of a shareholder declaration to remit those earnings. No further distributions with respect to pre-Merger earnings are due.

Outlook and Contingencies

Recently issued accounting standards

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ("SFAS") No. 133, *Accounting for Derivative Instruments and Hedging Activities*, which establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as "Derivatives") and for hedging activities. This statement requires that an entity recognize all derivatives as either assets or liabilities in the balance sheet and measure those instruments at fair value. The statement also sets forth the criteria for determining whether a derivative may be specifically designated as a hedge of a particular exposure. SFAS No. 133 is effective for all fiscal quarters of fiscal years beginning after June 15, 1999. The Company does not believe the adoption of SFAS 133 will have a material impact on the consolidated financial statements.

Euro

Fifteen European countries (the "Members") have joined together to form the European Union ("EU") whose purpose is to provide a forum to promote cooperation and better communication within the European community as well as with other countries outside of the EU. Eleven of the Members (the "Participating Members") have agreed to a plan to use a common currency ("euro") which became effective in January 1999. In preparation for adoption of the common currency, the Participating Members established certain credit and other criteria for participation. The Participating Members met all the criteria, agreed to participate, were approved by the other Members to participate, and adopted the euro as the common legal currency as of January 1, 1999. The Participating Members also established fixed conversion rates between their existing sovereign currencies (the "legacy currencies") and the euro. The euro trades on currency exchanges and is available for non-cash transactions. Participating Members will issue sovereign debt exclusively in euro and have redenominated outstanding sovereign debt. In addition, the Participating Members have granted authority for monetary policy, including money supply and official interest rates for the euro to the new European Central Bank. The legacy currencies of the Participating Members will remain legal tender in the Participating Members' countries as denominations of the euro between January 1, 1999 and December 31, 2001 (the "transition period"). Public and private parties may pay for goods and services during the transition period using either euros or the Participating Members' legacy currency. However, conversion rates will no longer be computed directly from one legacy currency to another. Instead, an amount denominated in one legacy currency will be converted into an amount denominated in euros with the resultant euro-denominated amount then being converted into the second legacy currency. Beginning January 1, 2002, the Participating Members will issue new euro-denominated bills and coins for use in cash transactions. By July 1, 2002 all Participating Members must have withdrawn all bills and coins denominated in the legacy currencies so that the legacy currencies will no longer be legal tender, making conversion to the euro complete. Germany, FMC's country of domicile is a Participating Member.

Currently, the Company has the ability to invoice, pay for goods and services and complete banking transactions in euros. The Company also plans to have all internal reporting entities situated in Participating Member countries to submit their reports in euros by the end of 1999. The euro conversion may affect cross-border competition by creating cross-border price transparency. Given the nature of the Company's business, customers may not have the luxury to "shop" cross-border given the nature of their illness, the type of reimbursement program they are enrolled in and the fact that they maintain a medical relationship with their supplier, a doctor/clinic. FMC's currency risk and risk management for operations in participating countries may be reduced as the legacy currencies are converted to euro. Final accounting, tax and governmental legal and regulatory guidance generally has not been provided in final form. The Company will continue to evaluate issues involving introduction of the euro.

Year 2000

The "Year 2000 problem" is the result of computer programs using two digits rather than four to define the applicable years. Such software may recognize a date using "00" as the year 1900 rather than the year 2000. These programs are present in software applications running on desktop computers and network servers. These programs are also present in microchips and microcontrollers incorporated into equipment. Certain of the Company's computer hardware and software, building infrastructure components (e.g. alarm systems, HVAC systems, etc.) and medical devices that are date sensitive may contain programs with the Year 2000 problem. If uncorrected, the problem could result in computer system and program failures or equipment and medical device malfunctions or miscalculations that could result in a disruption of business operations, billing and reimbursement breakdowns or affect patient treatment. If the Company, its significant customers, reimbursement sources or suppliers fail to make necessary modifications and conversions on a timely basis, the Year 2000 problem could have a material adverse effect on the Company's operations and financial results. The Company believes that its competitors face a similar risk.

The Company has been working on identifying and addressing potential Year 2000 risks since March 1997. In an effort to more comprehensively monitor and assess its progress in addressing Year 2000 issues, the Company established a Year 2000 Steering Committee. The committee is comprised of senior Company executives who meet regularly and provide status updates to the Company's management board on a regular basis. The Year 2000 issue is being evaluated for its internal effects for which the Company has reasonable control and on the external effects which will be based upon the capabilities of outside parties, such as suppliers, vendors, and other third parties.

Regarding information technology ("IT") systems, the Company is currently implementing a plan to inventory substantially all IT systems (e.g. clinical, supply chain management, financial, etc.) and is assessing Year 2000 compliance for those systems. The Company is developing specific plans and timetables to remediate or replace critical non-compliant systems. The Company is in the process of implementing an integrated financial/manufacturing/controlling system which is Year 2000 compliant. It is expected that this implementation will be completed by June 30, 1999. The Company's current target is to resolve Year 2000 compliance issues (including testing to validate Year 2000 compliance) for all critical IT systems by September 30, 1999.

Regarding non-IT equipment that may be dependent upon embedded software (e.g. medical, manufacturing/distribution, etc.), the Company has inventoried and assessed Year 2000 compliance for most of this equipment. The Company plans to have assessed Year 2000 compliance for all of its non-IT equipment by March 31, 1999. For medical equipment, the Company has developed specific plans to remediate Year 2000 non-compliance and is in the process of completing this remediation. For manufacturing/distribution equipment, the Company is in the process of developing specific plans to remediate Year 2000 non-compliance for this equipment. The Company's current target is to resolve Year 2000 compliance issues (including testing to validate Year 2000 compliance) for all non-IT equipment by September 30, 1999.

Although there can be no assurance that the Company will successfully complete implementation of its remediation efforts for IT systems and non-IT equipment by the dates critical for Year 2000 compliance, the Company's Year 2000 program is currently progressing in accordance with the Company's completion timetables. The Company relies heavily on third parties in operating its business. In addition to its reliance on systems and non-IT equipment vendors to verify Year 2000 compliance of their products, the Company also depends on 1) fiscal intermediaries which process claims and make payments for their Medicare and Medicaid programs, 2) insurance companies, HMOs, and other private payors, 3) utilities which provide electricity, water, natural gas, and telephone services, and 4) vendors of medical supplies and pharmaceuticals used in patient care. The Company is in the process of identifying and contacting all significant third parties to seek assurances that the third parties' services and products will not be interrupted or malfunction due to the Year 2000 problem. The Company intends to contact all significant third parties by March 31, 1999. The Company is in the process of contacting all significant third parties. Although the responses from these parties have been slow, the Company believes that it will still be able to obtain assurances of third party compliance to the year 2000 issue. Failure of significant third parties to resolve their Year 2000 issues could have a material adverse effect on the Company's results of operations and ability to provide health care service and manufacture products.

Costs related to the Year 2000 issue are funded through operating cash flows. The Company expects to spend a total of approximately $9 million in remediation and replacement efforts, including new software and hardware, costs to modify existing software, and consultant fees. The Company estimates remaining costs to be approximately $7 million. IT expenditures for Year 2000 are covered as part of the normal IT budget (the Year 2000 efforts are taking priority over other discretionary IT projects). Non-IT expenditures for Year 2000 are similarly being covered as part of the normal non-IT budget. The Company presently believes that the incremental cost of achieving Year 2000 compliant systems and equipment will not be material to the Company's financial condition, liquidity, or results of operation.

Time and cost estimates are based on currently available information. Developments that could affect estimates include, but are not limited to: 1) the availability and cost of trained personnel, 2) the ability to locate and correct all relevant computer code and systems, and 3) remediation success of the Company's customers and suppliers.

Based on its assessments to date, the Company believes it will not experience any material disruption as a result of Year 2000 issues in its internally manufactured medical devices, its internal manufacturing and distribution processes, and its internal information processing. However, if certain critical third party providers, such as those supplying electricity or water, experience difficulties resulting in disruption of service to the Company, a shutdown of the Company's operations at individual facilities could occur for the duration of the disruption.

The Year 2000 Steering Committee is completing its review of the various risk areas which might require a contingency plan. The committee is considering the need to develop contingency plans for certain key risk areas. At this point in time, the committee has not identified any risk areas which appear to have a reasonable likelihood to cause a material disruption to the Company's operations, although published reports have described a low level of Year 2000 compliance by Medicare and Medicard. Contingency plans will be developed on a case-by-case basis if new risks are identified or the Company's remediation/replacement efforts do not progress satisfactorily. Despite these efforts, judgements regarding contingency plans such as to what extent they should be developed are themselves subject to many variables and uncertainties. There can be no assurance that the Company will correctly anticipate the level, impact or duration of noncompliance by third party vendors or suppliers that provide inadequate information in respect to their Year 2000 status. As a result, there can be no assurance that any contingency plan developed by the Company will be sufficient to mitigate the impact of non-compliance by third-party vendors and service providers, and some material adverse effect to the Company could result regardless of such contingency plans. Nonetheless, the Company will continue to track its progress and will develop additional contingency plans if new risks are identified or the Company's remediation/replacement efforts do not progress satisfactorily.

Inflation

The effects of inflation during the periods covered by the consolidated financial statements have not been significant to Fresenius Medical Care's results of operations. However, most of Fresenius Medical Care's net revenues from dialysis care are subject to reimbursement rates regulated by governmental authorities, and a significant portion of other revenues, especially revenues from the U.S., is received from customers whose revenues are subject to such regulated reimbursement rates. Non-governmental payors are also exerting downward pressure on reimbursement rates. Increased operation costs that are subject to inflation, such as labor and supply costs, may not be recoverable through price increases in the absence of a compensating increase in reimbursement rates payable to Fresenius Medical Care and its customers and could materially adversely effect Fresenius Medical Care's business results of operations.

Quantitative and Qualitative Disclosures About Market Rate Risks

Management of Currency and Interest Rate Risks

The Company is primarily exposed to market risk from changes in foreign currency exchange rates and changes in interest rates. In order to manage the risks from such foreign currency exchange rate and interest rate fluctuations, the Company enters into various hedging transactions with investment grade financial institutions as authorized by the Management Board. The Company does not contract for financial instruments for trading or other speculative purposes.

The Company's financial instrument activity is consolidated under the control of a single centralized department. The Company has established guidelines for risk assessment procedures and controls for the use of financial instruments. They include a clear segregation of duties with regard to trading on one side and execution, accounting and controlling on the other.

Foreign Currency Exposure

Fresenius Medical Care conducts its business on a global basis in several major international currencies, although its operations are located principally in Germany and the United States. For financial reporting purposes, Fresenius Medical Care has chosen the U.S. dollar as its reporting currency. Therefore, changes in the rate of exchange between the U.S. dollar, euro and the local currencies in which the financial statements of its international operations, including those in Germany, are maintained, affect Fresenius Medical Care's results of operations and financial position as reported in its consolidated financial statements. FMC has consolidated the balance sheets of its non-U.S. dollar denominated operations into U.S. dollars at the exchange rates prevailing at the balance sheet date. Revenues and expenses are translated at the average exchange rates for the period.

The Company's exposure to market risk for changes in foreign exchange rates relates to transactions such as sales and purchases, lendings and borrowings. The Company sells significant amounts of products from its manufacturing facilities in Germany to its other international operations. In general, the Company's German sales are denominated in Deutsche Mark. Accordingly, the Company's subsidiaries are exposed to fluctuations in the rate of exchange between the Deutsche Mark and the currency in which their local operations are conducted. The Company employs, to a limited extent, forward contracts to hedge its currency exposures. The adoption of the euro as of January 1, 1999 by eleven of the countries in the European Union ("EU") should mitigate some of the fluctuations as the eleven countries begin trading in the common currency. The Company's policy, which has been consistently followed, is that forward currency contracts be utilized only for purposes of hedging foreign currency exposures. The Company has not used such instruments for purposes other than hedging.

The table below provides information about the Company's derivative foreign exchange instruments. The information is provided in U.S. dollar equivalent amounts. The table presents the notional amounts, the weighted average contractual foreign currency exchange rates, and the fair values of the contracts, which show the unrealized net gain (loss) on existing contracts as of December 31, 1998. All contracts are generally one to twenty four months in duration.

Foreign Currency Risk
December 31, 1998

Foreign Currency Forward	Notional Amount	Average Contract Rate DM	Fair Value Dec. 31 1998
Deutsche Mark	150,055	0.5840	1,587
British Pound	29,042	2.8885	1,021
Japanese Yen	25,600	0.1390	(1,693)
Australian Dollar	11,160	1.0889	694
New Zealand Dollar	3,287	0.8423	(120)
Singapore Dollar	4,218	1.0327	91
Purchase contracts	**223,362**		**1,580**
Deutsche Mark	49,752	0.5743	2,256
British Pound	6,496	2.8885	(111)
Other currencies	7,987	n.a.	317
Sale contracts	**64,235**		**2,462**

$ in thousands

A summary of the high and low exchange rates for Deutsche Mark to U.S. dollars and the average exchange rates for the last five years is set forth below:

Year ending December 31	Year's High	Year's Low	Year's Average	Year's Close
1994	0.6703	0.5663	0.6182	0.6452
1995	0.7384	0.6415	0.6989	0.6987
1996	0.6979	0.6395	0.6650	0.6432
1997	0.6468	0.5299	0.5764	0.5580
1998	0.6256	0.5395	0.5685	0.5977

Interest Rate Exposure

The Company is exposed to changes in interest rates as it relates to long-term borrowing. The Company enters into debt obligations and into receivables financings to support general corporate purposes including capital expenditures and working capital needs.

The Company's subsidiary NMC has entered into derivatives, particularly interest rate swap agreements and an interest rate collar agreement with various commercial banks for notional amounts totaling $ 1.6 billion as of December 31, 1998. All of these swap agreements were entered into for other than trading purposes. They effectively change NMC's interest rate exposure on the majority of its variable-rate revolving loans under the NMC Credit Facility ($ 1.0 billion outstanding as of December 31, 1998) and the drawdowns under the receivables financing facility (drawn as of December 31, 1998: $ 306 million) to fixed rates of interest between 6.05 % and 6.6025 %. The receivables financing facility has been reflected in the financial statements as a reduction to accounts receivable. These swap agreements expire at various dates between January 4, 2000 and January 5, 2004. At December 31, 1998, the fair value of these swap agreements and the interest rate collar agreement is ($ 51.5 million). The table below presents principal (or notional) amounts and related weighted average interest rates by year of maturity for the various interest rate agreements and the interest rate collar agreement for the Company's significant fixed-rate long-term debt obligations that are exposed to interest rate changes.

Interest Rate Exposure December 31, 1998	**1999**	**2000**	**2001**	**2002**	**2003**	**Thereafter**	**Totals**	**1998**
Principal payments on NMC Credit Facility Variable interest rate = 6.43 %	34	139	150	150	560		1,033	1,033
Interest rate derivative agreements Notional amount		850			500	250	1.600	52
Average fixed pay rate = 6.43%		6.37 %			6.60 %	6.12 %		
Receive rate = 3-month $ LIBOR								
Company obligated mandatorily redeemable preferred securities of subsidiary Fresenius Medical Care Capital Trusts Fixed interest rate = 9 %						360	360	374
Fixed interest rate = 7.875 %						450	450	446
Fixed interest rate = 7.375 %						179	179	182

$ in millions

Independent Auditors' Report

To the Shareholders
Fresenius Medical Care Aktiengesellschaft
Hof an der Saale, Germany:

We have audited the accompanying consolidated balance sheets of Fresenius Medical Care Aktiengesellschaft and subsidiaries ("the Company") as of December 31, 1998 and 1997 and the related consolidated statements of earnings, cash flows and shareholders' equity for each of the years in the three-year period ended December 31, 1998. These consolidated financial statements are the responsibility of the Company's management.
Our responsibility is to express an opinion on these consolidated financial statements based on our audits.
We conducted our audits in accordance with generally accepted auditing standards in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated 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. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.
In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 1998 and 1997, and the results of their operations and their cash flows for each of the three years in the three-year period ended December 31, 1998 in conformity with generally accepted accounting principles in the United States of America.
As discussed in Note 2 to the consolidated financial statements, the Company changed its method of accounting for start-up costs.

March 23, 1999
Frankfurt am Main, Germany

KPMG Deutsche Treuhandt-Gesellschaft
Aktiengesellschaft Wirtschaftsprüfungsgesellschaft

Consolidated Statements of Earnings

For the years ended December 31

	Note	1998	1997	1996
Net revenue				
Dialysis Care		2,358,577	1,901,189	434,342
Dialysis Products		1,147,099	1,073,180	985,193
		3,505,676	**2,974,369**	**1,419,535**
Cost of revenue				
Dialysis Care		1,568,192	1,238,612	298,640
Dialysis Products		637,394	647,874	561,443
		2,205,586	**1,886,486**	**860,083**
Gross profit		**1,300,090**	**1,087,883**	**559,452**
Operating expenses				
Selling, general and administrative		779,962	674,811	344,145
Research and development	2j	31,150	22,136	14,017
Operating income		488,978	390,936	201,290
Other (income) expense				
Interest income		(8,641)	(10,312)	(4,887)
Interest expense		228,182	193,860	61,475
Income from continuing operations before income taxes, minority interest and cumulative effect of accounting change		269,437	207,388	144,702
Income tax expense	2k	135,366	101,472	56,427
Income from continuing operations before minority interest and cumulative effect of accounting change		134,071	105,916	88,275
Minority interest		2,454	1,971	(1,125)
Income from continuing operations before cumulative effect of accounting change		131,617	103,945	89,400
Discontinued operations				
Loss from operations of discontinued businesses, net	5	(8,669)	(13,783)	(1,788)
Loss on disposal of businesses, net	5	(97,228)	–	–
Loss from discontinued operations, net	5	(105,897)	(13,783)	(1,788)
Income before cumulative effect of accounting change		25,720	90,162	87,612
Cumulative effect of accounting change, net	2u	(6,589)	–	–
Net income		**19,131**	**90,162**	**87,612**
Basic and fully diluted income from continuing operations before cumulative effect of accounting change per ordinary share	2s	1.62	1.34	2.00
Basic and fully diluted net income per ordinary share	2s	**0.20**	**1.16**	**1.96**
Basic and fully diluted income from continuing operations before cumulative effect of accounting change per preference share	2s	1.78	1.39	2.07
Basic and fully diluted net income per preference share	2s	**0.36**	**1.21**	**2.03**

$ in thousands, except share data
See accompanying notes to consolidated financial statements

Consolidated Balance Sheets

At December 31, 1998 and 1997

	Note	1998	1997
Assets			
Current assets			
Cash and cash equivalents	2c, 20	31,867	37,818
Trade accounts receivable, less allowance for doubtful accounts of $ 78,167 in 1998 and $ 75,653 in 1997	6, 20	590,125	498,273
Accounts receivable from related parties	3	48,031	35,730
Inventories	2d, 7	297,449	246,815
Prepaid expenses and other current assets		135,741	120,798
Net assets of discontinued operations	5	149,950	370,677
Deferred taxes	13	170,931	108,797
Total current assets		**1,424,094**	**1,418,908**
Property, plant and equipment, net	2e, 8	631,546	675,405
Intangible assets, including goodwill, net	2f	3,483,913	3,343,291
Investments in unconsolidated subsidiaries		19,307	36,657
Deferred taxes	13	23,188	5,344
Other assets		97,371	61,428
Total assets		**5,679,419**	**5,541,033**
Liabilites and shareholders' equity			
Current liabilities			
Accounts payable	20	149,502	156,258
Accounts payable to related parties	3	93,195	77,504
Accrued expenses and other current liabilities	11	443,123	431,256
Short-term borrowings	10	108,827	86,764
Short-term borrowings from related parties	3	60,000	66,428
Current portion of long-term debt and capital lease obligations	12	45,931	16,579
Income tax payable	2k, 20	57,077	29,063
Deferred taxes	13	17,975	6,176
Total current liabilities		**975,630**	**870,028**
Long-term debt and capital lease obligations, less current portion	12, 20	1,081,080	1,640,991
Other liabilities		17,129	15,580
Pension liabilities	2q, 14	49,759	41,576
Deferred taxes	13	190,005	147,182
Company obligated mandatorily redeemable preferred securities of subsidiary Fresenius Medical Care Capital Trusts holding solely Company guaranteed debentures of subsidiary at December 31, 1998 and Company debentures at December 31, 1997	15, 20	988,904	360,000
Minority interest	16	19,946	19,711
Total liabilities		**3,322,453**	**3,095,068**
Shareholders' equity	17		
Ordinary shares, DM 5 nominal value, 70,000,000 shares authorized, issued and outstanding		229,237	229,237
Preference shares, DM 5 nominal value, 42,500,000 shares authorized, 9,023,341 issued and outstanding at December 31, 1998 and 40,000,000 shares authorized, 9,023,341 issued and outstanding at December 31, 1997, respectively		27,590	27,590
Convertible investment securities		–	67,584
Additional paid-in capital		2,096,051	2,099,066
Retained earnings		80,078	108,875
Accumulated other comprehensive loss		(75,990)	(86,387)
Total shareholders' equity		**2,356,966**	**2,445,965**
Total liabilities and shareholders' equity		**5,679,419**	**5,541,033**

$ in thousands, except share data
See accompanying notes to consolidated financial statements

Consolidated Statement of Cash Flows

For the years ended December 31, 1998,1997 and 1996

	Note	1998	1997	1996
Operating activities				
Net income		19,131	90,162	87,612
Adjustments to reconcile net income to net cash and cash equivalents provided by (used in) operating activities				
Cumulative effect of accounting change		6,589	–	–
Depreciation and amortization		278,984	250,388	91,190
Loss from operations of discontinued businesses		8,669	13,783	1,788
Loss on disposition of businesses		97,228	–	–
Change in deferred taxes, net		23,586	13,275	(4,024)
Loss (gain) on sale of fixed assets		213	(1,703)	792
Changes in assets and liabilities, net of amounts from businesses acquired or disposed of				
Trade accounts receivable, net		(160,051)	(101,480)	(62,251)
Inventories		(39,304)	9,953	(25,099)
Prepaid expenses, other current and non-current assets		(37,295)	(8,920)	4,346
Accounts receivable from/payable to related parties		3,174	(19,835)	17,770
Accounts payable, accrued expenses and other current and non-current liabilities		(6,336)	(32,788)	5,208
Income taxes payable		73,669	3,053	561
Net cash provided by operating activities of continuing operations		268,257	215,888	117,893
Net cash used in operating activities of discontinued operations		(257)	(21,628)	(10,536)
Net cash provided by operating activities		268,000	194,260	107,357
Investing activities				
Purchases of property, plant and equipment	4, 22	(158,695)	(208,855)	(119,196)
Proceeds from sale of property, plant and equipment		26,179	776	27,983
Cash acquired, net of expenditures for acquisitions of NMC and minority interest in FUSA		–	–	185,792
Acquisitions and investments, net of cash acquired	4, 22	(222,935)	(424,599)	(4,085)
Proceeds from disposition of businesses		82,500	–	–
Net cash (used in) provided by investing activities of continuing operations		(272,951)	(632,678)	90,494
Net cash used in investing activities of discontinued operations		(7,315)	(20,171)	(3,518)
Net cash (used in) provided by investing activities		(280,266)	(652,849)	86,976
Financing activities				
Proceeds from short-term borrowings		54,954	89,287	150,578
Repayments of short-term borrowings		(44,795)	(124,470)	(121,227)
Proceeds from short-term borrowings from related parties		60,000	100,000	–
Repayments of short-term borrowings from related parties		(66,428)	(33,572)	–
Proceeds from long-term debt and capital lease obligations		60,150	253,426	96,562
Principal payments of long-term debt and capital lease obligations		(640,497)	(81,217)	(971,689)
Procceds from issuance of common stock by subsidiary		–	–	23,999
Retirement of convertible investment securities		(61,725)	–	–
Proceeds from issuance of mandatorily redeemable preferred securities		597,810	–	350,495
Proceeds from issuance of preference shares		–	168,774	419,567
Advances from and dividends to W.R. Grace		–	–	(10,060)
Proceeds from increase of accounts receivable securitization program		105,600	52,000	–
Proceeds from exercise of FMC Rollover options		1,047	4,903	–
Dividends paid		(49,214)	–	–
Distributions on convertible investment securities		(2,752)	(1,302)	–
Net activity with Fresenius AG		–	–	(69,522)
Change in minority interest		717	954	(1,125)
Net cash provided by (used in) financing activities of continuing operations		14,867	428,783	(132,422)
Net cash used in financing activities of discontinued operations		(2,107)	(4,462)	(9,890)
Net cash provided by (used in) financing activities		12,760	424,321	(142,312)
Effect of exchange rate changes on cash and cash equivalents	2h	(6,445)	8,449	(475)
Cash and cash equivalents				
Net (decrease) increase in cash and cash equivalents		(5,951)	(25,819)	51,546
Cash and cash equivalents at beginning of period		37,818	63,637	12,091
Cash and cash equivalents at end of period		**31,867**	**37,818**	**63,637**

$ in thousands

See accompanying notes to consolidated finacial statements

Consolidated Statements of Shareholders' Equity

For the years ended December 31, 1998, 1997 and 1996

	Note	Ordinary Shares		Preference Shares				Accumulated			
		Number of Shares	Amount	Number of Shares	Amount	Convertible investment securities	Additional paid in-capital	Retained Earnings	Other Comprehensive Loss	Net Assets	Total
Balance at December 31, 1995		**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**305,625**	**305,625**
Contribution of Fresenius Worldwide Dialysis to Fresenius Medical Care for ordinary shares, nominal value DM 5		35,210,000	115,307	–	–	–	229,723	–	–	(345,030)	–
Contribution of Fresenius USA minority interest to Fresenius Medical Care for ordinary shares, nominal value DM 5		3,430,000	11,233	–	–	–	223,979	–	–	–	235,212
Contribution of Fresenius National Medical Care Holdings to Fresenius Medical Care for ordinary shares, nominal value DM 5		31,360,000	102,697	–	–	–	1,073,395	–	–	–	1,176,092
Issuance of preference shares, nominal value DM 5, net of expenses		–	–	5,400,000	17,684	–	401,883	–	–	–	419,567
Adjustment for intercompany receivable/payable reported as a component of net assets at December 31, 1995		–	–	–	–	–	(31,502)	–	–	–	(31,502)
Net activity with Fresenius AG		–	–	–	–	–	–	–	–	(16,488)	(16,488)
Comprehensive income	2r										
Net income		–	–	–	–	–	–	20,015	–	67,597	87,612
Foreign currency translation adjustment	2h	–	–	–	–	–	–	–	(8,318)	(11,704)	(20,022)
Comprehensive income		–	–	–	–	–	–	–	–	–	67,590
Balance at December 31, 1996		**70,000,000**	**229,237**	**5,400,000**	**17,684**	**–**	**1,897,478**	**20,015**	**(8,318)**	**–**	**2,156,096**
Proceeds from issuance of preference shares		–	–	3,623,341	9,906	–	193,293	–	–	–	203,199
Proceeds from issuance of convertible investment securities		–	–	–	–	67,584	–	–	–	–	67,584
Contributed capital from Fresenius AG		–	–	–	–	–	3,392	–	–	–	3,392
Proceeds from exercise of FMC Rollover options		–	–	–	–	–	4,903	–	–	–	4,903
Distributions on convertible investment securities		–	–	–	–	–	–	(1,302)	–	–	(1,302)
Comprehensive income	2r										
Net income		–	–	–	–	–	–	90,162	–	–	90,162
Foreign currency translation adjustment	2h	–	–	–	–	–	–	–	(78,069)	–	(78,069)
Comprehensive income		–	–	–	–	–	–	–	–	–	12,093
Balance at December 31, 1997		**70,000,000**	**229,237**	**9,023,341**	**27,590**	**67,584**	**2,099,066**	**108,875**	**(86,387)**	**–**	**2,445,965**
Proceeds from exercise of FMC Rollover options		–	–	–	–	–	1,047	–	–	–	1,047
Retirement of convertible investment securities		–	–	–	–	(67,584)	–	–	–	–	(67,584)
Distributions on convertible investment securities		–	–	–	–	–	–	(2,752)	–	–	(2,752)
Distributions to Fresenius AG		–	–	–	–	–	(4,062)	–	–	–	(4,062)
Dividends paid		–	–	–	–	–	–	(45,176)	–	–	(45,176)
Comprehensive income	2r										
Net income		–	–	–	–	–	–	19,131	–	–	19,131
Foreign currency translation adjustment	2h	–	–	–	–	–	–	–	10,397	–	10,397
Comprehensive income		–	–	–	–	–	–	–	–	–	29,528
Balance at December 31, 1998		**70,000,000**	**229,237**	**9,023,341**	**27,590**	**–**	**2,096,051**	**80,078**	**(75,990)**	**–**	**2,356,966**

$ in thousands, except share data

See accompanying notes to consolidated financial statements

1. The Company, Merger and Basis of Presentation

The Company

Fresenius Medical Care Aktiengesellschaft ("FMC" or the "Company") was formed in a series of transactions constituting the "Merger" (described hereunder) consummated on September 30, 1996 by Fresenius Aktiengesellschaft ("Fresenius AG") and W.R. Grace & Co ("W.R. Grace"). Prior to formation, FMC was originally incorporated as "Sterilpharma GmbH", a wholly owned subsidiary of Fresenius AG. Prior to the Merger, Sterilpharma's name was changed to Fresenius Medical Care GmbH and in conjunction with the Merger it was converted into a German stock corporation (Aktiengesellschaft) and renamed "Fresenius Medical Care Aktiengesellschaft".

FMC is an integrated provider of dialysis products and care.

The Merger

The Merger, which was effective on September 30, 1996, represented consummation of an Agreement and Plan of Reorganization entered into on February 4, 1996 by Fresenius AG and W.R. Grace. In the Merger, Fresenius AG contributed Fresenius Worldwide Dialysis ("FWD"), representing its global dialysis business (including its controlling interest in Fresenius USA, Inc.), to FMC in exchange for 35,210,000 ordinary shares. Thereafter, FMC acquired (i) all of the outstanding common stock of W.R. Grace, whose sole business at the time of the transaction represented National Medical Care, Inc. ("NMC"), the global dialysis business of W.R. Grace, which subsequently was renamed Fresenius National Medical Care Holdings, Inc. ("FNMC"), and (ii) the minority interest of Fresenius USA, Inc. ("FUSA") not otherwise held by Fresenius AG in exchange for 31,360,000 ordinary shares and 3,430,000 ordinary shares, respectively. The foregoing W.R. Grace and FUSA ordinary share amounts included approximately 217,000 and 116,000 ordinary shares, respectively, reserved for issuance to holders of FUSA and W.R. Grace stock options (see Note 18) and approximately 324,000 ordinary shares reserved for issuance to holders of FUSA warrants.
Additionally, in conjunction with the Merger, each holder of W.R. Grace common stock received one share of a Class D Preferred stock of FNMC for each share of stock previously held. The Class D Preferred stock entitles the holder to receive, when, if and as declared by the board of directors of FNMC, a special dividend, payable in cash in annual installments beginning on October, 2002 (and in each subsequent year until the dividend is fully paid) in an amount based on the adjusted cash flow, as defined in the terms of the Class D Preferred Stock, of Fresenius Medical Care AG for the period from January 1, 1997 to December 31, 2001.
At June 12, 1997, FNMC, by vote of its shareholders, changed its name to Fresenius Medical Care Holdings, Inc. ("FMCH").

Accounting for the Merger

Immediately prior to formation of FMC, Fresenius AG owned a majority of the common shares of each of the businesses constituting FWD and after formation of FMC, Fresenius AG owns a majority of the ordinary shares of FMC. The contribution of the businesses constituting FWD into FMC in exchange for ordinary shares has been accounted for as a combination of entities under common control. Accordingly, the assets and liabilities of the businesses constituting FWD contributed to FMC have been recorded by FMC at their historical cost (predecessor basis).
The issuances by FMC of ordinary shares for (i) all of the common shares of FMCH and (ii) the FUSA minority shareholders' interest in FUSA, have been accounted for as acquisitions using the purchase method of accounting. Accordingly, the fair value of each acquisition has been allocated to the assets acquired, including intangibles, and liabilities assumed (or in the case of the FUSA acquisition, the proportionate share of such amounts acquired and assumed). The fair value assigned to the FMCH acquisition was approximately $ 1,152,000 and was based upon the mid-point of a range of values assigned to the businesses by independent financial advisors to Fresenius AG. The fair value of the FUSA acquisition of $ 236,547 was determined by reference to the quoted market price of the FUSA common shares. The excess of the fair value of each acquisition over the fair value of the assets acquired and liabilities assumed, was approximately $ 1,697,000 for the FMCH acquisition, and $ 232,779 for the FUSA acquisition, each of which is being amortized over a 40 year period.
Dividends payable, if any, in the future by FMCH under the series D preferred stock will be accounted for as additional purchase price consideration for FMCH by FMC.
In connection with recording the liabilities assumed in the acquisition of FMCH, the Company recorded approximately $ 123,000 for preacquisition contingencies primarily related to litigation and related legal costs. These adjustments resulted from discussions with the United States government in March 1997. The anticipated legal costs were accrued at the low end of a range of values and the ultimate costs could be significantly higher. The Company is in discussions with the United States government and other parties regarding certain of the matters discussed in Note 19. Any difference between any final settlement and the Company's estimate will be charged to operations. In 1996, the Company has also accrued approximately $ 50,000 for certain costs, principally severance payments and lease commitments, related to the closing of certain FMCH manufacturing and distribution operations as well as the closing of certain clinics of the Homecare business. At December 31, 1998, approximately $ 62,000 in payments and other charges have been applied against the preacquisition contingencies and $ 40,000 against the restructuring contingency.
The results of operations of FMCH and the results of operations of the minority share of the operations of FUSA acquired have been included in FMC's operations from October 1, 1996.
The following unaudited pro forma summary presents the consolidated results of continuing operations of FMC as if the Merger had been completed as of the beginning of 1996, after giving effect to certain adjustments, including depreciation and amortization of the assets acquired based upon their fair values, increased interest expense from the financing and refinancing of the acquisition and income tax effects. Pro forma net income per ordinary share and pro forma net income per preference share have been calculated as if all shares outstanding at December 31, 1996 were outstanding as of the beginning that year. This pro forma summary does not necessarily reflect the results of operations of the Company as they would have been if the acquisition had been completed as of the beginning of such periods, does not include the acquisitions

discussed in Note 4 and is not necessarily indicative of the results which may be obtained in the future.

Year ended December 31, 1996	
Net revenue	2,690
Net income Basic and fully diluted net	44
Income per ordinary share Basic and fully diluted net	0.58
Income per preference share	0.65

$ in millions, except share data

Basis of Presentation
The accompanying consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles ("U.S. GAAP"). The accompanying consolidated statements of earnings, cash flows and shareholders' equity for the year ended December 31, 1996 include the combined historical financial statements of FWD, including Sterilpharma GmbH, assuming that FWD, during that time a business unit of Fresenius AG, was organized during the period presented as a separate legal entity, owning certain net assets and certain subsidiaries and associated companies of Fresenius AG.

2. Summary of Significant Accounting Policies

(a) Principles of consolidation
The consolidated financial statements include all material companies in which the Company has legal or effective control. All significant intercompany transactions and balances have been eliminated. The equity method of accounting is used for investments in associated companies (20 % to 50 % owned).

(b) Classifications
Certain non-material items in prior years' consolidated financial statements have been reclassified to conform with the current year's presentation.

(c) Cash and cash equivalents
Cash and cash equivalents represent cash and certificates of deposit with original maturity dates of three months or less at origination.

(d) Inventories
Inventories are stated at the lower of cost (determined by using the average or first-in, first-out method) or market value.

(e) Property, plant and equipment
Property, plant, and equipment are stated at cost. Significant improvements are capitalized; repairs and maintenance costs that do not extend the useful lives of the assets are charged to expense as incurred. Property and equipment under capital leases are stated at the present value of future minimum lease payments at the inception of the lease. The cost and accumulated depreciation of assets sold or otherwise disposed are removed from the accounts, and any resulting gain or loss is included in income when the assets are disposed.
Depreciation on property, plant and equipment is calculated using the straight-line method over the estimated useful lives of the assets ranging from 10 to 50 years for buildings and improvements and 3 to 15 years for machinery and equipment. Equipment held under capital leases and leasehold improvements are amortized using the straight-line method generally over the shorter of the lease term or the estimated useful life of the asset.
The Company capitalizes interest on borrowed funds during construction periods. Interest capitalized during 1998, 1997, and 1996 was $ 221, $ 51, and $ 638, respectively.

(f) Intangible assets
The Company has adopted the following useful lives and amortizes intangible assets using the straight-line method: goodwill - 20 to 40 years; patents - 17 years; patient relationships, distribution rights and other intangible assets - over the estimated period to be benefited, generally from 2 to 6 years.
The Company assesses the recoverability of its intangible assets by determining whether the amortization of the asset's balance over its remaining useful life can be recovered through projected undiscounted cash flows.

(g) Derivative financial instruments
The Company utilizes derivative financial instruments including forward currency contracts and interest rate swaps.

Forward currency contracts
Gains and losses on forward currency contracts that are designated and effective as hedges of existing assets, liabilities and firm commitments are deferred and recognized along with the effects of the hedged transaction. Gains and losses on other forward currency contracts are recognized as selling, general and administrative expenses in the period in which the gain or loss occurs.

Interest rate swaps
Interest rate agreements that are designated as a hedge of a debt or other long-term obligations are accounted for on an accrual basis. That is, the interest payable and interest receivable under the terms of the swaps are accrued and recorded as an adjustment to the interest or related expense of the designated liability or obligation. Amounts due from and payable to the counterparties of interest rate swaps are recorded on an accrual basis at each reporting date on amounts computed by reference to the respective interest rate swap contract. Realized gains and losses that occur from the early termination or expiration of contracts are deferred and recorded in income over the remaining period of the original swap agreement. Gains and losses arising from interest differential on contracts that hedge specific borrowings are recorded as a component of interest expense over the life of the contract.
The effectiveness of the hedge is measured by a historical and probable future high correlation of changes in the fair value of the hedging instruments with changes in the value of the hedged item. If correlation ceases to exist, hedge accounting will be terminated and gains or losses recorded in other income.

(h) Foreign currency translation
For purposes of these consolidated financial statements, the U.S. dollar has been used as the reporting currency.
The Company follows the provisions of Statement of Financial Accounting Standards ("SFAS") No. 52, *Foreign Currency Translation*. Substantially all assets and liabilities of the Company and all Non-U.S. subsidiaries are translated at year end exchange rates, while revenues and expenses are translated at exchange rates prevailing during the year. Adjustments for foreign currency translation fluctuations are excluded from net earnings and are included in other comprehensive income.
Gains and losses resulting from the translation of intercompany borrowings, which are not considered equity investments, are included in selling, general and administrative expense. Translation gains amounted to $ 366, $ 28,286 and $ 1,943 for 1998, 1997 and 1996, respectively. Gains and losses arising from interest differential on contracts that hedge specific borrowings are recorded as a component of interest expense over the life of the contract.

(i) Revenue recognition policy
Product revenues are recognized when title to the product has passed to the buyer, either at the time of shipment or upon receipt by the customer. Health care revenues are recognized on the date services and related products are provided and are recorded at amounts estimated to be received under reimbursement arrangements with third-party payors.

(j) Research and development expenses
Research and development expenses are expensed as incurred.

(k) Income taxes
Prior to the Merger, the Company consisted of wholly owned subsidiaries of Fresenius AG and as such did not file separate income tax returns in Germany, Austria, Great Britain, Belgium, Japan, or Brazil. In such cases, the Company's income tax provision has been computed as if it were a separate company. In the United States, Switzerland, France, Italy, The Netherlands and Spain, the Company operated as a separate subsidiary of Fresenius AG and, as such, filed income tax returns in such countries. Income taxes payable in the accompanying consolidated balance sheets relate solely to tax liabilities of the Company's subsidiaries in countries where the subsidiary files an income tax return. Subsequent to the Merger, the Company files its own separate income tax returns in substantially all jurisdictions.
In accordance with SFAS No. 109, *Accounting for Income Taxes*, deferred tax assets and liabilities are recognized for the future consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Deferred taxes in Germany are calculated using the "undistributed earnings" tax rate (see Note 13).

(l) Impairment
In accordance with Statement of Financial Accounting Standards No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of*, the Company reviews the carrying value of its investments for impairment whenever events or changes in circumstances indicate that the carrying amount of assets may not be recoverable. The Company considers various valuation factors including discounted cash flows, fair values and replacement costs to assess any impairment of goodwill and other long lived assets.

(m) Debt issuance costs
Costs related to the issuance of debt are amortized over the term of the related obligation using the straight line method.

(n) Self-insurance programs
A major subsidiary of the Company is self-insured for professional, product and general liability, auto and workers' compensation claims up to predetermined amounts above which third party insurance applies. Estimates include ultimate costs for both reported claims and incurred but not reported.

(o) Use of estimates
The preparation of consolidated financial statements 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 consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(p) Concentration of credit risk
The Company is engaged in the manufacture and sale of products for all forms of kidney dialysis equipment, principally to health care providers throughout the world, and the providing of kidney dialysis treatment, clinical laboratory testing and other medical ancillary services. The Company performs ongoing credit evaluations of its customers' financial condition and, generally, requires no collateral from its customers.
A significant percentage of the Company's health care services revenues are paid by and subject to regulations under governmental programs, primarily Medicare and Medicaid, health care programs administered by the United States government. The Company reserves for losses related to these programs, including uncollectable accounts receivable.

(q) Pension and other postretirement benefits
Effective December 31, 1998, the Company adopted SFAS No. 132, *Employers' Disclosures about Pensions and Other Postretirement Benefits*. The provisions of SFAS No. 132 revise employers' disclosures about pension and other postretirement benefit plans. It does not change the measurement or recognition of these plans. It standardized the disclosure requirements for pensions and other post retirement benefits to the extent practicable.

(r) Comprehensive income
The Company adopted the provisions of SFAS No. 130, *Reporting Comprehensive Income*, effective January 1, 1998. This statement requires that all items that are required to be recognized under accounting standards as components of comprehensive income be reported in a financial statement that is displayed with the same prominence as other financial statements. This statement further

requires that the Company classify items of other comprehensive income by their nature in a financial statement and display the accumulated balance of other comprehensive income separately from retained earnings and additional paid-in capital in the equity section of a statement of financial position.

(s) Earnings per ordinary and preference share

In 1997, the Company adopted the provisions of SFAS No. 128, *Earnings Per Share*. All prior periods have been restated to reflect the provisions of SFAS No. 128. This statement requires the presentation of basic earnings per share and diluted earnings per share. Basic earnings per share are computed by dividing net income less preference amounts and distributions earned by convertible investment securities by the weighted average number of ordinary and preference shares outstanding during the year. Diluted earnings per share includes the effect of all potentially dilutive ordinary and preference shares that would have been outstanding during the year. Prior to October 1, 1996, when FMC consisted solely of FWD, including FUSA, basic net income per ordinary share has been calculated assuming that the 35,210,000 ordinary shares Fresenius AG received in the Merger were issued and outstanding. Basic net income per ordinary share and basic net income per preference share for the years ended December 31, 1998, 1997, and 1996 have been calculated using the two-class method required under U.S. GAAP based upon the weighted average number of ordinary and preference shares outstanding.
The convertible investment securities (see Note 17) and awards granted under the FMC stock incentive plans (see Note 18) are potentially dilutive equity instruments.

(t) Stock option plans

The Company accounts for its stock option plans in accordance with the provisions of Accounting Principles Board ("APB") Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations. As such, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeds the exercise price. On January 1, 1996, the Company adopted the disclosure only provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*. The Company has elected to continue to apply the provisions of APB Opinion No. 25 and provide the pro forma disclosure provisions of SFAS No. 123.

(u) Accounting changes

In April 1998, Statement of Position No. 98-5, *Reporting on the Costs of Start-up Activities* ("SOP 98-5"), was issued by the Accounting Standards Executive Committee (AcSEC) of the AICPA and was adopted by the Company, effective January 1, 1998. SOP 98-5 requires that the costs of start-up activities, including organization costs, which have been previously capitalized, should be expensed as incurred. As a result of the adoption of SOP 98-5, deferred start-up activities in the amount of $ 11,279 as of January 1, 1998, have been recognized as a cumulative effect of a change in accounting, net of related tax benefit of $ 4,690, in the consolidated statements of earnings for the year ended December 31, 1998. Costs for start-up activities were expensed as incurred during 1998.

(v) Transfers and servicing of financial assets and extinguishments of liabilities

In June 1996, the Financial Accounting Standards Board issued SFAS No. 125, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. SFAS No. 125 is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after December 31, 1996 and is to be applied prospectively. This Statement provides accounting and reporting standards for transfers and servicing of financial assets and extinguishments of liabilities based on consistent application of a financial-components approach that focuses on control.
It distinguishes transfers of financial assets that are sales from transfers that are secured borrowings. There was no material effect on net income as a result of applying this standard.

3. Related Party Transactions

During 1998 and 1997, there were certain intercompany and related party transactions recorded as a result of the services performed as noted below. Intercompany transactions are generally settled according to their respective terms and are eliminated in consolidation. Related party transactions pertaining to services performed between affiliated entities are recorded as accounts receivable or payable to related parties. At December 31, 1998 and 1997, FMC had accounts receivable from related parties of $ 48,031 and $ 35,730, respectively. The FMC accounts payable to related parties at December 31, 1998 and 1997 were $ 93,195 and $ 77,504, respectively.

(a) Shared production facilities

Prior to the Merger discussed in Note 1, FMC shared certain manufacturing facilities with Fresenius AG's non-FMC businesses. In connection with the Merger, in each situation where facilities were shared, post-Merger ownership of the location or manufacturing facility (collectively, the "Facilities") was retained by Fresenius AG or contributed to FMC. Prior to the Merger, production and related services rendered by FMC at shared Facilities to Fresenius AG were effectively allocated to Fresenius AG at fully absorbed cost and, accordingly, were accounted for as an inventory transfer through the consolidated statement of earnings. Such production rendered by Fresenius AG at shared Facilities on behalf of FMC was also effectively allocated to FMC at fully absorbed cost. For the year ended December 31, 1996 the aggregate costs that were allocated to Fresenius AG by FMC for production and related services at shared Facilities were $ 16,513 while the aggregate production costs that were allocated to FMC from Fresenius AG for the year ended December 31, 1996 were $ 26,877. In conjunction with the Merger, the Company entered into contractual agreements with Fresenius AG to sell to and purchase production from Fresenius AG at current market prices.

(b) Real estate located in Germany

Under the terms of the Merger, certain land and manufacturing and office buildings located in Germany were retained by Fresenius AG and leased to FMC under operating lease agreements. Accordingly, such land and buildings are excluded from the accompanying consolidated balance sheets. The accompanying consolidated statements of earnings include for the year ended December 31, 1996, $ 1,157 of depreciation expense related to such facilities representing an assumed charge to FMC from Fresenius AG for the use of the land and buildings.

Under the operating lease agreements entered into in conjunction with the Merger, FMC will pay Fresenius AG approximately DM 16,800 per year. Beginning in 1998, the lease amounts escalate annually, based upon the German cost of living index for a four person employee household, representing a fair market value rental for such properties. Converted to USD, this amounts to approximately $ 10,101, $ 9,684 and $ 10,805 at December 31, 1998, 1997 and 1996, respectively. The leases have terms of 10 years with options for renewal.

(c) Shared services

Fresenius AG historically provided services to and incurred costs on behalf of the Company. In addition, FMC has provided certain services to Fresenius AG. The costs of such services, including, but not limited to, administrative services, management information services, employee benefit administration, legal and environmental consultation and administration insurance, central purchasing, tax services, treasury services, and accounting and reporting have been allocated to the Company. The allocation of the costs and expenses for services from Fresenius AG to FMC's operations was $ 41,931 for the year ended December 31, 1996. The allocation of the costs and expenses for services from FMC to Fresenius AG was $ 16,529 for the year ended December 31, 1996. These allocations were based upon service contracts between the relevant parties as well as upon methods that management believes are reasonable, including the use of time estimates, headcount and transaction statistics, and similar activity-based data. In the opinion of management of the Company, such expenses are indicative of the actual expenses that would have been incurred if the Company had been operating as an independent entity.

In connection with the Merger, the Company entered into service agreements with Fresenius AG to continue to receive the foregoing services at negotiated amounts. For the years 1998 and 1997, amounts charged from Fresenius AG to FMC under the terms of the agreement are $ 21,298 and $ 17,517, respectively. FMC charged amounts of $ 5,233 and $ 5,858 for services rendered to Fresenius AG in 1998 and 1997, respectively.

(d) Financing provided by Fresenius AG

During the years ended December 31, 1998 and 1997, the Company borrowed $ 60,000 and $ 100,000, respectively, at an interest rate of 6.53 % for 1998 and at a range of interest rates between 4.53 % and 5.125 % for 1997. The funds were used for general corporate purposes. At December 31, 1998, the balance was $ 60,000 and is due in March, 1999. At December 31, 1997 the balance which was due and paid in March 1998, was $ 66,428, in DM denominated funds. Interest paid on these borrowings was $ 1,096 and $ 6,000 for the years 1998 and 1997, respectively.

(e) Sales to Fresenius AG and its subsidiaries

During the years ended December 31, 1998, 1997, and 1996, the Company recognized sales of $ 13,237, $ 22,874, and $ 15,530, respectively, to non-FMC businesses of Fresenius AG.

(f) Financial support

Prior to the Merger, Fresenius AG provided substantial financial support to FUSA, a majority owned entity included within FWD. This support included guarantees of letters of credit in connection with FUSA's previously outstanding industrial revenue bonds, providing credit support to assist in securing lines of credit, participating in and assisting with foreign exchange contracts as well as various miscellaneous general management assistance.

(g) Other

A member of the Company's Supervisory Board is a partner in a law firm which provided services to the Company. The Company paid the law firm approximately $ 254, $ 554, and $ 299 in 1998, 1997, and 1996, respectively. The Chairman of the Company's Supervisory Board, who was the former Chief Executive Officer of FMC, as well as the current Chief Executive Officer of FMC are members of the Management Board of Fresenius AG, the majority shareholder of FMC.

4. Acquisitions

The Company acquired certain health care facilities and clinical laboratories for a total consideration of $265 million and $527 million in 1998 and 1997, respectively. In 1998, the consideration consisted of cash of $223 million and convertible investment securities classified as a liability of $42 million. The consideration in 1997 was $425 million in cash and the remainder of $102 million was in convertible investment securities and preference shares. These acquisitions have been accounted for as purchase transactions and, accordingly, are included in the results of operations from the dates of acquisition. The excess of the total acquisition costs over the fair value of the tangible net assets acquired was $243 million and $436 million for 1998 and 1997, respectively.

Had the acquisitions occurring in 1997 been consummated at January 1, 1997, unaudited pro forma net revenue from continuing operations would have been $3,096 million and unaudited pro forma net income $99 million for the twelve months ended December 31, 1997. Unaudited pro forma basic and diluted net income per ordinary share and per preference share would have been $1.19 and $1.25, respectively.

Had the acquisitions occurring in 1997 and the Merger (see Note 1) been consummated at January 1, 1996, unaudited pro forma net revenue from continuing operations would have been $2,968 million and unaudited pro forma net income $55 million for the twelve months ended December 31, 1996. Unaudited pro forma basic and diluted net income per ordinary share and per preference share would have been $.63 and $.70, respectively.

Management considers the pro forma adjustments for the acquisitions which occurred in 1998 and 1996, except for the Merger, to be insignificant.

5. Discontinued Operations

Effective June 1, 1998, the Company classified its Homecare/non-renal Diagnostics businesses as discontinued operations. The sale of the non-renal Diagnostics business was completed on June 26, 1998 while the sale of the Homecare business was completed on July 29, 1998. In connection with the sale of Homecare, the Company retained the assets and the operations associated with the delivery of IDPN and records, for accounting purposes, its activity as part of discontinued operations. The Company has recorded net after tax losses of $9 million from operations of discontinued businesses and $97 million from the disposal of these businesses for the year ended December 31, 1998. The net loss on the disposal of these businesses and their results of operations have been accounted for as discontinued operations and are being disclosed separately in these financial statements. Prior periods have been reclassified to reflect the impact of discontinued operations. The remaining assets and liabilities have been classified in the consolidated balance sheet as net assets of discontinued operations.

Discontinued operations - results of operations

The revenue and results of operations of the discontinued operations were as follows:

For the year ended December 31	1998	1997
Net revenue	120,940	283,006
Cost of revenue	73,950	161,556
Gross profit	46,990	121,450
Selling, general and administrative	61,202	142,451
Loss from operations of discontinued businesses before income tax benefit	(14,212)	(21,001)
Income tax benefit	(5,543)	(7,218)
Loss from operations of discontinued businesses	(8,669)	(13,783)
Loss on disposal before income tax benefit	(140,000)	–
Income tax benefit	(42,772)	–
Loss on disposal	(97,228)	–
Loss from discontinued operations	**(105,897)**	**(13,783)**

$ in thousands

Discontinued operations - consolidated balance sheet

The net assets of the discontinued operations of the Homecare/non-renal Diagnostics businesses, included in the consolidated balance sheet at December 31, are as follows:

	1998	1997
Current assets	168,005	294,138
Properties and equipment, net	219	61,131
Other assets	593	52,435
Total assets	**168,817**	**407,704**
Current liabilities	18,620	35,144
Other liabilities	247	1,883
Total liabilities	**18,867**	**37,027**
Net assets	**149,950**	**370,677**

$ in thousands

Included in current assets of discontinued operations is approximately $150 million of net Intradialytic Parenteral Nutrition ("IDPN") receivables.

These assets have not been sold and will remain classified as discontinued operations until they have been settled (see Note 19).

6. Sale of Accounts Receivable

The Company had an agreement with a bank to sell up to $ 200,000 of an undivided interest in a designated pool of accounts receivable. On September 27, 1997, a new $ 204,000 agreement was established with another bank to replace the existing agreement. The facility was amended on February 27, 1998 to increase the commitment amount to $ 331,500. The current agreement has an effective interest rate of 5.30 % and matures on September 27, 1999 (see Note 20). At December 31, 1998 and 1997, $ 305,600 and $ 200,000, respectively, had been received pursuant to such sales and are reflected as reductions to accounts receivable. Under the terms of the agreement, new interests in accounts receivable are sold as collections reduce previously sold accounts receivable. The costs related to such sales are expensed as incurred and recorded as interest expense and related financing costs. There were no gains or losses on these transactions.

7. Inventories

As of December 31, inventories consisted of the following:

	1998	1997
Raw materials and purchased components	63,404	60,073
Work in process	29,326	35,166
Finished goods	182,865	124,215
	275,595	**219,454**
Health care supplies	31,828	35,620
Reserves	(9,974)	(8,259)
Inventories	**297,449**	**246,815**

$ in thousands

Under the terms of certain unconditional purchase commitments, the Company is obligated to purchase materials during 1999 amounting to $ 70,460.

8. Property, Plant and Equipment

As of December 31, property, plant and equipment consisted of the following:

	1998	1997
Land and improvements	8,560	8,858
Buildings and improvements	296,553	235,810
Machinery and equipment	580,955	639,889
Machinery, equipment and rental equipment under capitalized leases	23,126	28,460
Construction in progress	42,678	42,287
	951,872	955,304
Accumulated depreciation and amortization	(320,326)	(279,899)
Property, plant and equipment, net	**631,546**	**675,405**

$ in thousands

Depreciation and amortization expense for property, plant and equipment, including, for periods prior to the Merger, amounts related to real estate in Germany (see Note 3), amounted to $ 130,628, $ 120,540, and $ 56,399 for the years ended December 31, 1998, 1997, and 1996, respectively.

Included in property, plant and equipment as of December 31, 1998 and 1997 were $ 36,996 and $ 32,198, respectively, of peritoneal dialysis cycler machines which the Company leases to customers with end-stage renal disease on a month-to-month basis and hemodialysis machines which the Company leases to physicians under operating leases. Identification of the rental income from the Company's leasing activities is not practicable as the Company's return on the machines is received through contractual arrangements whereby a premium is charged for other support equipment sold during the life of the lease.

Accumulated depreciation related to machinery, equipment and rental equipment under capital leases was $ 10,785, $ 16,067 and $ 21,383 at December 31, 1998, 1997 and 1996, respectively.

Operating leases

The Company leases buildings and machinery and equipment under various lease agreements expiring on dates through 2010. Rental expense recorded for operating leases for the years ended December 31, 1998, 1997, and 1996 was $ 122,459, $ 99,429, and $ 40,393, respectively.

In September 1997, FUSA amended a sale and leaseback arrangement with a bank that covers the sale by FUSA of approximately $ 40,100 of certain new equipment of FUSA's dialyzer manufacturing facility at its Ogden, Utah plant. The agreement has an expiration date of January 1, 2010, with renewal options and a purchase option. If FUSA elects not to purchase the equipment or renew the lease at the end of the lease term, FUSA will be obligated to pay a remarketing fee of up to $ 1,350.

Future minimum rental payments under noncancelable operating leases for the five years succeeding December 31, 1998 are:

1999	98,256
2000	85,363
2001	76,369
2002	56,188
2003	49,628
Thereafter	148,846
	514,650

$ in thousands

9. Intangible Assets, net

As of December 31, intangible assets consisted of the following:

	1998	1997
Goodwill	3,020,123	2,903,568
Patient relationships	173,604	166,726
Patents	266,919	257,949
Distribution rights	6,601	2,411
Other	343,086	209,569
	3,810,333	**3,540,223**
Accumulated amortization	(326,420)	(196,932)
Intangible assets, net	**3,483,913**	**3,343,291**

$ in thousands

Amortization expense for intangible assets amounted to $147,616, $127,297, and $32,528 for the years ended December 31, 1998, 1997 and 1996 respectively (see note 2(f)).

10. Short-Term Borrowings

Short-term borrowings of $108,827 and $86,764 at December 31, 1998 and 1997, respectively, represent amounts borrowed by certain of the Company's subsidiaries under lines of credit with commercial banks. The average interest rates on these borrowings at December 31, 1998 and 1997 was 4.2% and 5.0%, respectively.

Excluding amounts available under the NMC Credit Facility (see Note 12), at December 31, 1998, FMC had $35,932 available under such commercial bank agreements. These lines of credit are generally secured by the Company's accounts receivable and contain various covenants including, but not limited to, requirements for maintaining defined levels of working capital, net worth, capital expenditures and various financial ratios.

11. Accrued Expenses and Other Current Liabilities

As at December 31, accrued expenses and other current liabilities consisted of the following:

	1998	1997
Accrued legal and compliance costs	51,319	66,678
Accrued insurance	66,321	65,903
Accrued salaries and wages	68,875	59,635
Outstanding credit memos	42,804	41,455
Accrued interest	44,933	36,786
Accrued restructuring	10,651	24,034
Accrued physician compensation	18,321	18,646
Bonus and incentive plan compensation	4,302	11,258
Tax liabilities	14,366	11,104
Lease liabilities	3,345	5,998
Commissions	12,061	5,639
Deferred Income	7,470	7,335
Accrued other	98,355	76,785
Total accrued expenses and other current liabilities	**443,123**	**431,256**

$ in thousands

12. Long-Term Debt and Capital Lease Obligations

As of December 31, long-term debt and capital lease obligations consisted of the following:

December 31	1998	1997
NMC Credit Facility	1,032,700	1,613,300
Capital leases	15,126	27,935
Other	79,185	16,335
	1,127,011	**1,657,570**
Less current maturities	(45,931)	(16,579)
	1,081,080	**1,640,991**

$ in thousands

Immediately prior to the Merger, NMC entered into a credit agreement with a group of banks (collectively, "the Lenders"), pursuant to which the Lenders made available to NMC and certain specified subsidiaries and affiliates an aggregate of $2,500,000 through three credit facilities (collectively, the "NMC Credit Facility"). The NMC Credit Facility, as amended, originally included (i) a revolving credit facility of up to $1,000,000 for up to seven years (of which up to $250,000 is available for letters of credit, up to $450,000 is available for borrowings in certain non-U.S. currencies, up to $50,000 is available as swing lines in U.S. dollars and up to $20,000 is available as swing lines in certain non-U.S. currencies) ("Facility 1"); (ii) a term loan facility of $1,000,000 for up to seven years ("Facility 2"); and (iii) a term loan facility of $500,000 for up to two years ("Facility 3").

Loans under the NMC Credit Facility bear interest at one of the following rates, at (i) LIBOR plus an applicable margin or (ii) a base rate equal to the sum of (1) the higher from time to time of (A) the prime rate of the Lenders or (B) the federal funds rate plus 0.50% and (2) an applicable margin. A fee is payable to the Lenders equal to a percentage per annum (initially 0.375%) of the portion of the NMC Credit Facility not used.

In addition to scheduled principal payments, the NMC Credit Facility will be reduced by certain portions of the net cash proceeds from certain sales of assets, sales of accounts receivable and the issuance of subordinated debt and equity securities. All payments outstanding under Facility 1 are due and payable at the end of the seventh year. Prepayments are permitted at any time without penalty, except in certain defined periods. The NMC Credit Agreement contains customary affirmative and negative covenants with respect to the Company, NMC and its subsidiaries. Further, certain of the Company's subsidiaries are not permitted to make payments of dividends or other distributions of certain classes of stock except in certain limited circumstances.

In November 1996, Facility 3 was fully repaid by the Company, effectively reducing the Company's credit line to $2 billion, $1 billion for Facility 1 and $1 billion for Facility 2.

In February, 1998, the Company issued Company obligated mandatorily redeemable Trust Preferred Securities in the amount of $450,000 and DM 300,000. Part of the proceeds, $250,000, was utilized to permanently reduce Facility 2 of the Credit Agreement. Under the Credit Agreement, the repayment schedule will be ratably reduced (see Note 15).

At December 31, 1998, the Company had $ 507,578 of additional borrowing capacity available under Facility 1 of the NMC Credit Facility including $ 40,278, for additional letters of credit. Of the $ 209,722 letters of credit outstanding under the NMC Credit Facility, a $ 150,000 irrevocable letter of credit was issued to the U.S. Government pursuant to the OIG Agreement (see Note 19).
Future minimum lease payments under capital leases as of December 31, 1998 are:

1999	10,457
2000	4,867
2001	491
2002	300
2003	284
Thereafter	522
	16,921
Amounts representing interest	(1,795)
Present value capital lease obligations	15,126
Current portion of capital lease obligations	(9,287)
Capital lease obligations, less current portion	**5,839**

$ in thousands

Interest rates on capital lease obligations at December 31, 1998 range from 6.5 % to 12 % and were imputed based on the lower of the Company's incremental borrowing rate at the inception of the lease or the lessor's implicit rate.
Aggregate annual payments applicable to the NMC Credit Facility, term loan, note payable, capital leases and other borrowings for the five years subsequent to December 31, 1998 are:

1999	45,931
2000	153,301
2001	152,683
2002	151,773
2003	561,954
Thereafter	61,369
	1,127,011

$ in thousands

13. Income Taxes

Income before income taxes, minority interest, and cumulative effect of accounting change is attributable to the following geographic locations:

	1998	1997	1996
Germany	70,877	73,663	92,044
United States	118,574	87,764	33,294
Other	79,986	45,961	19,364
	269,437	**207,388**	**144,702**

$ in thousands

income tax expense (benefit) for the years ended December 31 consisted of the following:

	1998	1997	1996
Current			
German corporation and trade income taxes	25,266	34,593	44,136
United States income taxes	54,600	40,541	5,286
	79,866	**75,134**	**49,422**
Deferred			
Germany	15,281	1,964	(1,088)
United States	16,800	12,605	1,762
	32,081	**14,569**	**674**
Other	23,419	11,769	6,331
	135,366	**101,472**	**56,427**

$ in thousands

German corporation tax law applies a split rate imputation system to the income taxation of a corporation and its shareholders. Upon distribution of retained earnings in the form of a dividend, shareholders subject to German tax receive a credit for corporation taxes paid by the corporation on such distributed earnings. In addition, the corporation receives a tax refund to the extent such earnings had been initially subjected to a corporation income tax in excess of 30 %. The tax refund is also distributable to the shareholder.
In general, retained German corporate income is initially subject to a federal corporation income tax currently at 45 % plus a surcharge of 5.5 % on the federal corporate tax payable. Giving effect to the surcharge, the federal corporate tax rate is 47.475 %. The distributed earnings rate is 31.65 % as a result of the surcharge.
For purpose of computing the 1996 income tax expense for the Company's German operations, a complete distribution of the year's earnings is assumed. For 1998 and 1997, the income tax expense reflects the actual amount of distribution of that year's earnings of the German operations. As such, the refund of tax described above is reflected in the income tax expense reconciliation presented below.
For the years ended December 31, 1998, 1997, and 1996 income tax expense differed from the amounts computed by applying the German federal corporation income tax rate of 47.475 % for 1998 and 48.375 % for 1997 and 1996, respectively, to income before

income taxes, minority interest and cumulative effect of accounting change as a result of the following:

	1998	1997	1996
Computed "expected" income tax expense at the undistributed earnings rate continuing operations before minority interest and cumulative effect of accounting change	127,929	100,324	70,000
Increase (decrease) in income taxes resulting from			
Items not deductible for tax purposes	843	801	381
Dividend distributions credit	(5,803)	(7,455)	(16,759)
Trade income taxes, net of German federal corporation income tax benefit	8,351	8,467	5,996
Tax charge (benefit) for certain transactions not (previously) taken	844	(2,844)	–
Foreign tax rate differential	3,727	2,895	(2,774)
Other	(525)	(716)	(417)
Provision for income taxes	**135,366**	**101,472**	**56,427**
Effective tax rate continuing operations before minority interest and cumulative effect of accounting change	**50.2 %**	**48.9 %**	**39.0 %**

$ in thousands

During 1998 and 1997, the valuation allowance decreased by $ 15,436 and $ 8,957, respectively, primarily attributable to a change in management's evaluation of future utilization of operating losses in 1998 and utilization of operating losses by FMCH in 1997.
At December 31, 1998 and 1997, FMC had approximately $ 48,854 and $ 77,712, respectively, of net operating losses outside of the U.S., the majority of which are not subject to an expiration period. There was also a net operating loss carry forward of approximately $ 37,329 in the U.S. attributable to FUSA. The FUSA net operating losses expire in varying amounts beginning in 1997 through 2010. The ability of the Company to use the carry forwards to offset taxes on its future income is also subject to limitations.
In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities and projected future taxable income in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not the Company will realize the benefits of these deductible differences, net of the existing valuation allowances at December 31, 1998.
Provision has not been made for additional taxes on $ 52,450 for undistributed earnings of subsidiaries. The majority of these

The tax effects of the temporary differences that give rise to deferred tax assets and liabilities at December 31 are presented below:

	1998	1997
Deferred tax assets		
Accounts receivable, primarily due to allowance for doubtful accounts	29,591	17,252
Inventory, primarily due to additional costs capitalized for tax purposes, and inventory reserve accounts	18,068	8,939
Reserves for financial accounting purposes, not currently tax deductible	132,185	109,920
Capital leases, principally due to capitalization of costs for tax purposes	5	3,580
Discontinued operations	–	5,861
Net operating loss carryforwards	36,698	24,059
Other	918	1,768
Total deferred tax assets	**217,465**	**171,379**
Less: valuation allowance	(5,340)	(20,776)
Net deferred tax assets	**212,125**	**150,603**
Deferred tax liabilities		
Accounts receivable, primarily due to allowance for doubtful accounts	2,892	2,052
Inventory, primarily due to additional costs capitalized for tax purposes, and inventory reserve accounts	5,929	–
Reserves for financial accounting purposes, not currently taxable	36,019	1,469
Plant and equipment, principally due to differences in depreciation	178,704	186,258
Other	2,442	41
Total deferred tax liabilities	**225,986**	**189,820**
Net deferred tax liabilites	**(13,861)**	**(39,217)**

$ in thousands

earnings have been, and will continue to be, reinvested. The earnings could become subject to additional tax if they were remitted as dividends, if funds were granted as loans to the Company or an affiliate in the amount of retained earnings, or if the Company should sell its stock in the subsidiaries. The Company estimates that the distribution of these earnings would result in $ 2,029 of additional withholding and federal income taxes.

Intraperiod tax allocation

Income tax expense was allocated among the following items as follows:

	1998	1997	1996
Continuing operations	135,366	101,472	56,427
Operations of discontinued operations	(5,543)	(7,218)	(1,242)
Disposal of discontinued businesses	(42,772)	–	–
Total income tax expense	**87,051**	**94,254**	**55,185**

$ in thousands

14. Employee Benefit Plans

Defined benefit pension plans

Prior to the Merger, the Company's employees participated in various Fresenius AG pension plans. In connection with the Merger, the Company established separate plans for its employees on terms substantially equivalent to the Fresenius AG plans. Additionally, FMCH provides pension benefits to substantially all of its employees. Plan benefits are generally based on employee years of service and final salary. Consistent with normal business custom in the Federal Republic of Germany, FMC's pension obligations in Germany are unfunded. In the United States, substantially all U.S. employees are covered by NMC's non-contributory, defined benefit pension plan. Each year, NMC contributes to this plan at least the minimum amount required by law. Plan assets consist principally of publicly traded common stock, fixed income securities and cash equivalents. In addition, NMC also sponsors a supplemental executive retirement plan to provide certain key executives with benefits in excess of normal pension benefits.

The following provides a reconciliation of benefit obligations, plan assets, and funded status of the plans.

	1998	1997	1996
Change in benefit obligation			
Benefit obligation at beginning of year	88,713	79,609	
Translation loss (gain)	1,432	(2,242)	
Service cost	8,905	8,484	
Interest cost	6,418	5,589	
Actuarial loss (gain)	9,400	(1,897)	
Divestitures	(1,717)	–	
Benefits paid	(1,319)	(830)	
Benefit obligation at end of year	**111,832**	**88,713**	
Change on plan assets			
Fair value of plan assets at beginning of year	65,088	54,218	
Actual return on plan assets	13,218	11,794	
Benefits paid	(1,287)	(924)	
Fair value of plan assets at end of year	**77,019**	**65,088**	
Funded status	(34,813)	(23,625)	
Unrecognized net gain	(11,821)	(15,328)	
Unrecognized transition obligation	475	531	
Accrued benefit costs	**(46,159)**	**(38,422)**	
Weighted-average assumptions as of December 31,			
Discount rate	6.59 %	7.41 %	7.20 %
Expected return of plan assets	9.70	9.00	9.00
Rate of compensation increase	4.60	4.60	4.60
Components of net period benefit cost			
Service cost	8,905	8,484	3,095
Interest cost	6,418	5,589	2,021
Expected return on plan assets	(6,430)	(4,758)	(1,103)
Amortization of transition obligation	56	184	–
Recognized net (gain)/loss	(857)	(231)	106
Curtailment net gain	(1,717)	–	–
Net periodic benefit costs	**6,375**	**9,268**	**4,119**

$ in thousands

In addition to the principal pension plans, certain of the Company's other subsidiaries offer separate retirement plans. The total accrued pension cost for these plans was $ 3,600, $ 3,154, and $ 2,866 at December 31, 1998, 1997 and 1996, respectively. The company does not provide any postretirement benefits to its employees other than those provided under its pension plans and supplemental executive retirement plan.

Defined contribution plans

NMC and FUSA sponsor defined contribution plans. Total contributions for the year ended December 31, 1998, and 1997 were $ 7,195 and $ 6,385, respectively, and $ 1,204 for the three-months ended December 31, 1996.

15. Mandatorily Redeemable Trust Preferred Securities

In November, 1996 the Company, through Fresenius Medical Care Capital Trust (the "1996 Trust"), a statutory business trust organized under the laws of the State of Delaware, issued $ 360,000 of 9 % Trust Preferred Securities (the "Trust Securities"). FMC owns all of the common securities of the 1996 Trust. The sole asset of the Trust is $ 360,500 aggregate principal amount of 9 % Senior Subordinated Debentures due 2006 of FMC Trust Finance S.à.r.l. Luxembourg, a wholly owned subsidiary of the Company ("Luxco"), and related guarantees by the Company, Fresenius Medical Care Deutschland GmbH ("D-GmbH") and Fresenius Medical Care Holdings, Inc. ("FMCH"), D-GmbH and FMCH being the "Subsidiary Guarantors". The Trust Securities are guaranteed by FMC through a series of undertakings by the Company and the Subsidiary Guarantors.

The Trust Securities entitle the holders to distributions payable at an annual rate of 9 % and are mandatorily redeemable on December 1, 2006. The holders of the Trust Securities are entitled upon liquidation of the 1996 Trust to a distribution equal to the stated amount of the Trust Securities. Except in limited circumstances, the holders of the Trust Securities have no voting rights.

Luxco has the right to redeem the 9 % Senior Subordinated Debenture, in whole or in part, at any time or from time to time after December 1, 2001, at specified redemption prices plus accrued and unpaid interest. In connection with any such redemption, the 1996 Trust must redeem a like amount of Trust Securities.

In February, 1998, the Company, through Fresenius Medical Care Capital Trust II ("Trust II") and Fresenius Medical Care Capital Trust III ("Trust III", and collectively with Trust II, "the 1998 Trusts"), statutory business trusts created under the laws of the State of Delaware, issued $ 450,000 of 7 7/8 % USD Trust Preferred Securities (the "Trust II Securities") and DM 300,000 of 7 3/8 % DM Trust Preferred Securities (the "Trust III Securities" and, together with the Trust II Securities, the "Trust Preferred Securities"). FMC owns all of the common securities of the 1998 Trusts. The sole asset of Trust II is $ 450,450 aggregate principal amount of Luxco 7 7/8 % USD Senior Subordinated Debentures due 2008 and related guarantees by the Subsidiary Guarantors. The sole asset of Trust III is DM 300,300 aggregate principal amount of Luxco 7 3/8 % DM Senior Subordinated Debentures due 2008 and related guarantees by the Subsidiary Guarantors. The Trust Preferred Securities are guaranteed by FMC through a series of undertakings by the Company and the Subsidiary Guarantors.

The Trust II and Trust III Securities entitle the holders to distributions payable at the annual rate of 7 7/8 % and 7 3/8 %, respectively, and are mandatorily redeemable on February 1, 2008. The holders of the Trust Preferred Securities are entitled, upon liquidation of the 1998 Trusts, to a distribution equal to the stated amount of the Trust Preferred Securities. Except in limited circumstances, the holders of the Trust Preferred Securities have no voting rights.

16. Minority Interest

At December 31, minority interests were as follows:

	1998	1997
FMCH Preferred Stock		
Preferred Stock, $100 par value		
6 % Cumulative; 40,000 shares authorized; 36,460 outstanding	3.646	3.646
8 % Cumulative Class A; 50,000 shares authorized; 16,176 outstanding	1.618	1.618
8 % Noncumulative Class B; 40,000 shares authorized; 21,483 outstanding	2.148	2.148
Preferred Stock, $ 0.10 par value		
Noncumulative Class D; 100,000,000 shares authorized; 89,061,590 outstanding	8.906	8.906
Sub-total FMCH minority interest	**16.318**	**16.318**
Other minority interest	3.628	3.393
Total minority interest	**19.946**	**19.711**

$ in thousands, except share data

17. Shareholders' Equity

The authorized, issued and outstanding share capital of FMC consists of 70 million ordinary shares with a nominal value of DM 5 per share and an aggregate nominal value of DM 350,000.
Under the German Stock Corporation Act, the shareholders of a stock corporation may empower the Managing Board to issue shares in a specified aggregate nominal value not exceeding 50 % of the issued share capital at the time of the passing of the resolution, in the form of Conditional Capital (Bedingtes Kapital) or Approved Capital (Genehmigtes Kapital). The authorization for the issuance of Approved Capital is limited for a period not exceeding five years from the date the shareholders' resolution becomes effective.
By way of a shareholders' resolution, FMC's Managing Board has been authorized to issue Approved Capital for cash ("Approved Capital I") up to a total of DM 70,000 nominal amount (14 million preference shares). In addition, for non-cash consideration in connection with acquisitions by FMC, up to a total of DM 105,000 (21 million preference shares) was approved ("Approved Capital II").
Shareholders' equity at December 31, 1995 represents the excess of assets over liabilities to unrelated third-parties of the business units included in FMC. Intercompany transactions and charges between FMC and Fresenius AG were also, effectively, accounted for within net activity with Fresenius AG.

During 1997 and 1996, the Company issued 3,623,341 and 5,400,000 preference shares, nominal value DM 5 per share, for net proceeds of $ 203,199 and $ 419,567, respectively. The preference shares issued rank equally with the ordinary shares with respect to liquidation rights and pre-emptive rights. The minimum annual dividend payable on the preference shares is 4 % of the shares' nominal value or DM 0.20 per year. The Company's Articles of Association also provide that the annual dividend paid on the preference shares must exceed the annual dividend of the ordinary shares by 2 % of the preference shares' nominal value or DM 0.10. Holders of preference shares have no voting right except in certain specific situations. The preference shares are not entitled to a preference in liquidation but rank pari passu with the ordinary shares. Of the 9,023,341 preference shares outstanding at December 31, 1997, 8,562,500 shares out of Approved Capital I are entitled to a dividend for the years 1996 and 1997, while the remaining 460,841 preference shares out of Approved Capital II are only entitled to a dividend for the year 1997.
Under the German Stock Corporation Act, the amount of dividends available for distribution to shareholders is based upon the retained earnings of Fresenius Medical Care AG as reported in its balance sheet determined in accordance with the German Commercial Code (Handelsgesetzbuch). At December 31, 1996, Fresenius Medical Care AG had no retained earnings available for dividend distribution.
In accordance with a contribution agreement between the Company and Fresenius AG, entered into in connection with the Agreement and Plan of Reorganization, the Company distributed $ 4,062 during the year ending December 31, 1998, to Fresenius AG. These funds represented earnings of the former Fresenius Worldwide Division (FWD) prior to the contribution of FWD by Fresenius AG to the Company as part of the Merger. These earnings were not distributed at the time of the Merger due to the application of local generally accepted accounting principles in determining the amount of pre-merger earnings and the legal requirement of a shareholder declaration to remit those earnings. In anticipation of a determination of the amount and a positive shareholder declaration, an estimate of the amount that would be due was made. The estimated amount was loaned by the Company to Fresenius AG with any distribution of earnings to be utilized to reduce the receivable from Fresenius AG. During 1998, the $ 4,062 distribution of earnings was subsequently applied against the receivable by the Company.
In 1998, the Managing Board recommended a dividend of DM 1.00 per ordinary share for the year 1997, DM 1.10 per preference share for the year 1997 and DM 0.20 per preference share for the year 1996. The Supervisory Board and shareholders of FMC approved the dividends which were paid in 1998.
In connection with certain acquisitions made during 1997, a subsidiary of the Company issued convertible investment securities (Wandel-Genußrechte) with a nominal (par) value of $ 67,584. The convertible investment securities, which are non-voting, carry a cumulative dividend rate between 6.12 % and 6.25 % payable only out of legally available earnings of FMC AG and are redeemable ten years from date of issuance. The Company and the convertible investment security holders also entered into agreements which permit the Company to exchange, and under certain circumstances permit the convertible investment security holders to request, that the Company exchange the convertible investment securities at the Company's option, for cash or for preference shares or other specified securities of an equal value. As the Company has the unilateral ability to exchange the convertible investment securities for preference shares and the preference shares represent permanent equity securities of the Company, the Company had classified the convertible investment securities within shareholders' equity. During the year ended December 31, 1998, the Company satisfied its obligations that became due relating to these equity securities obligations. A total of approximately $ 61,725 nominal amount of these securities were redeemed. Approximately $ 5,857 nominal amount of these securities remain outstanding and were reclassified as a liability at year end 1998. Management intends to redeem these securities when they come due with cash and/or other marketable securities.
In 1999, the Managing Board has recommended a dividend of DM 1.15 per ordinary share and DM 1.25 per preference share for the year 1998. If the Supervisory Board of FMC approves of the dividends, the shareholders will vote at the annual shareholders' meeting on the Supervisory Board recommendations. If no dividend is declared for two consecutive years after the year for which the preference shares are entitled to dividends, then the holders of such preference shares will be entitled to the same voting rights as holders of ordinary shares until all arrearages are paid. In addition, the payment of dividends by FMC is subject to limitations under the NMC Credit Agreement (see Note 12).

The following table is a reconciliation of the numerators and denominators of the basic and diluted earnings per share computations. The 1996 and 1998 stock option plans had no effect on the diluted earnings per share computations.

	1998	1997	1996
Weighted average number of			
ordinary shares outstanding	70,000,000	70,000,000	43,907,500
preference shares outstanding	9,023,341	6,506,917	517,808
potentially dilutive shares	2,522	–	–
Income from continuing operations before cumulative effect of accounting change	**131,617**	**103,945**	**89,400**
less:			
Distributions on convertible investment securities	(2,752)	(1,302)	–
Income from continuing operations before cumulative effect of accounting change	**128,865**	**102,643**	**89,400**
less:			
Dividend arrearages on preference shares for 1996 declared and paid in 1998	(974)	–	–
Preference for preference shares	(513)	(375)	(34)
Income from continuing operations before cumulative effect of accounting change available to all classes of shares	**127,378**	**102,268**	**89,366**
Loss from discontinued operations, net	(105,897)	(13,783)	(1,788)
Cumulative effect of accounting change	(6,589)	–	–
Basic and fully diluted income from continuing operations before cumulative effect of accounting change per ordinary share	1.62	1.34	2.00
Basic and fully diluted loss from discontinued operations per ordinary share	(1.34)	(0.18)	(0.04)
Basic and fully diluted cumulative effect of accounting change per ordinary share	(0.08)	–	–
preference and declared dividend arrearages per preference share	0.16	0.05	0.07
Basic and fully diluted income from continuing operations before cumulative effect of accounting change per preference share	1.78	1.39	2.07
Basic and fully diluted loss from discontinued operations per preference share	(1.34)	(0.18)	(0.04)
Basic and fully diluted cumulative effect of accounting change per preference share	(0.08)	–	–

$ in thousands, except share data

18. Stock Options

Prior to the Merger, FUSA provided a number of stock option plans (the "FUSA Plans") which granted its employees and officers options to purchase FUSA common stock. In connection with the Merger, a significant amount of such options was repurchased by FUSA. Certain options outstanding under FUSA's 1987 Stock Option Plan were exchanged for equivalent options with respect to FMC ordinary shares (the "FMC Rollover Plan").

Also in connection with the Merger, certain W.R.Grace stock options previously issued to employees of NMC ("NMC Plan") were exchanged for options to purchase FMC ordinary shares under the FMC Rollover Plan. The exercise prices established for the former FUSA and W.R. Grace options exchanged for FMC ordinary share options were based upon the FUSA and W.R. Grace option exercise prices multiplied by the respective share exchange ratios ("share exchange ratio") established in the Merger.

Approximately 313,000 FUSA options were exchanged for FMC options at the rate of one FUSA option for 1.112 FMC option, resulting in approximately 348,000 FMC options being issued. Each option was exercisable for $^1/_3$ of an ordinary share resulting in approximately 116,000 ordinary shares in total.

Approximately 198,000 NMC options were exchanged for FMC options at the rate of one NMC option for 3.25 FMC options, resulting in approximately 643,500 FMC options being issued. Each option was exercisable for $^1/_3$ of an ordinary share, resulting in approximately 214,500 ordinary shares in total.

The resulting total number of shares issuable upon exercise of options under the FMC Rollover Plan at the Merger date, September 30, 1996, was approximately 333,000. No additional ordinary shares are available for granting of options under the FMC Rollover Plan. In the Merger, the ordinary shares issuable upon exercise of FMC Rollover options were issued to Fresenius AG which is holding the shares pending exercise of the options. Fresenius AG has agreed, with respect to the ordinary shares underlying options related to W.R. Grace common stock, to not exercise voting power over such ordinary shares and to return any dividends paid. Upon exercise of any of the FMC Rollover options, the exercise price will be paid to the Company and Fresenius AG will deliver the ordinary shares to the option holder. Upon cancellation or expiration without exercise of options formerly relating to W.R. Grace common stock, the underlying ordinary shares held by Fresenius AG will be transferred to FMC at no cost to it. Upon cancellation or expiration without exercise of options formerly relating to FUSA common stock, the underlying ordinary shares held by Fresenius AG will revert to Fresenius AG. During the year ended December 31, 1998, 136,679 FMC Rollover Plan options were exercised by employees. In connection therewith, Fresenius AG transferred 45,560 ordinary shares to employees and remitted $ 1,047 to the Company. During the same period, 2,818 options were canceled. At December 31, 1998, the $ 1,047 has been accounted for as a capital contribution within additional paid in capital.

Immediately prior to the Merger, FMC adopted a stock incentive plan (the "FMC Plan") for FMC's key management and executive employees. Under the FMC Plan, eligible employees will have the right to acquire preference shares of the Company. Awards under the FMC Plan are evidenced by a non-transferable convertible bond and corresponding non-recourse loan to the employee, secured solely by the bond with which it was made. The bonds mature in ten years and are generally fully convertible after three or five years. Each convertible bond, which is DM denominated, entitles the holder thereof, upon payment of a conversion price equal to the fair market value of the preference shares on the award date, to convert the bond into a number of preference shares equal to the face amount of the bond divided by the preference shares' nominal value (DM 5 per preference share). During 1997, the Company granted 2,697,438 awards (of which 216,663 were forfeited in 1997) with a bond nominal value of DM 4,135 and exercisable upon vesting for 826,757 preference shares (net of forfeitures). No awards were granted during 1996, the first year of the FMC Plan. The awards issued and forfeited during 1997 and outstanding as of December 31, 1997 had a weighted average price of $ 76.03 per preference share. During 1998, 2,169,711 awards were cancelled or forfeited, leaving 311,064 awards outstanding under this plan. If these awards are exercised, a total of approximatly 103,688 preference shares would be issued. At December 31, 1998, 34,174 awards were exercisable under the FMC Plan.

During 1998, the Company adopted two new stock incentive plans ("FMC 98 Plan 1" and "FMC 98 Plan 2") for FMC's key management and executive employees. Under FMC 98 Plan 1, eligible employees have the right to acquire preference shares of the Company. Grants for these rights (the "Grants") under FMC 98 Plan 1 will be evidenced by a non-transferable convertible bond and corresponding non-recourse loan to the employee, secured solely by the bond with which it was made. The bonds mature in ten years and are generally fully convertible after three or five years. Each convertible bond, which is DM denominated, entitles the holder thereof, upon payment of a conversion price equal to the fair market value of the preference shares one day after the grant date, to convert the bond into a number of preference shares equal to the face amount of the bond divided by the preference shares' nominal value (DM 5 per preference share). The maximum number of preference shares that may be issued under this plan is 1,333,333 less any shares issued, or subject to issue, under the FMC Plan. Any shares available due to forfeiture of Grants under the FMC Plan would be considered available under FMC 98 Plan 1 as long as the total preference shares issued under both plans does not exceed the 1,333,333 shares noted above. During 1998, the Company awarded 1,024,083 Grants with a bond nominal value of DM 5,120,415 and exercisable upon vesting for 1,024,083 preference shares. At December 31, 1998, there were 205,562 preference shares for which Grants could be issued. No Grants were exercisable under FMC 98 Plan 1 at December 31, 1998. Under FMC 98 Plan 2, eligible employees will have the right to acquire preference shares (the "Options") of the Company. The share price of the preference share shall be equal to the average of the official daily quotation prices of the preference shares on the Frankfurt Stock Exchange on the thirty days (30) of trading immediately prior to the date of grant of the award. One third of an option vests on each of the second, third and fourth anniversary of the award date, provided that the Company achieves certain performance criteria for the full fiscal year following the grant date in comparison to its performance for the full fiscal year preceding the grant date. The term of FMC 98 Plan 2 is five years and not more than 20 % of the total options available under the plan may be issued in any year. Options granted under FMC 98 Plan 2

have a 10-year term. The maximum number of preference shares that may be issued under this plan is 2,500,000 shares, of which 500,000 are designated for Managing Board members and 2,000,000 are for other managerial staff. During 1998, the Company awarded 258,314 options with a nominal value of DM 1,291,570.
At December 31, 1998, no options were exercisable under FMC 98 Plan 2.

The following table shows the number of shares available and average price range for each stock options plan:

	Shares in thousands	**Average price range** in $
FUSA and NMC Plans		
Opening balance at September 30, 1996	333	8.43 - 46.53
Exercised	35	9.78 - 41.07
Forfeited	3	36.69 - 41.07
Exercisable at December 31, 1996	295	8.43 - 46.53
Exercised	126	9.78 - 41.07
Forfeited	1	39.06 - 41.07
Exercisable at December 31, 1997	168	8.43 - 46.53
Exercised	46	16.98 - 70.12
Forfeited	1	70.12 - 70.12
Exercisable at December 31, 1998	121	14.39 - 70.12
FMC Plan		
Balance at December 31, 1996	–	
Granted	899	55.59 - 78.33
Forfeited	72	55.59 - 78.33
Balance at December 31, 1997	827	55.59 - 78.33
Forfeited	723	55.59 - 78.33
Balance at December 31, 1998	104	55.59 - 78.33
FMC Plan 1		
Balance at December 31, 1997	–	
Granted	1,024	40.91 - 57.29
Balance at December 31, 1998	1,024	40.91 - 57.29
FMC Plan 2		
Balance at December 31, 1997	–	
Granted	258	48.92
Balance at December 31, 1998	258	48.92

Fair value stock options
The per share weighted-average fair value of stock options granted during 1998 was $ 18.41 on the date of grant using the binominal option-pricing model with the following weighted-average assumptions: expected dividend yield ranging from 1.39 % to 2.11 %, risk-free interest rate ranging from 3.78 % to 4.74 %, expected volatility of 35 % and an expected life of 5.3 years.
The per share weighted-average fair value of stock options granted during 1997 was $ 27.82 on the date of grant using the binominal option-pricing model with the following weighted-average assumptions: expected dividend yield 1.0 %, risk-free interest rate of 5.0 %, expected volatility of 35 % and an expected life of 5.3 years.
The Company applies APB Opinion No. 25 in accounting for stock compensation and, accordingly, no compensation cost has been recognized for its stock options in the consolidated financial statements. Prior to 1998, no stock options had been granted which would have resulted in significant compensation costs under SFAS No. 123. Had the Company determined compensation cost based on the fair value at the grant date for its stock options under SFAS No. 123, the Company's 1998 net income would have been reduced to the pro forma amounts indicated below:

	1998	**1997**
Net income		
As reported	19,131	90,162
Effect of FMC Plan benefit (expense)	1,726	(4,103)
Effect of FMC 98 Plans (expense)	(2,967)	–
Pro forma	17,890	86,059
Basic and diluted net income per Ordinary share		
As reported	0.20	1.16
Pro forma	0.18	1.11
Preference share		
As reported	0.36	1.21
Pro forma	0.34	1.16

$ in thousands, except share data

The Company revised its estimates of compensation costs for the FMC Plan due to the large amount of forfeitures and cancellations that occurred in 1998. This resulted in a significant reduction in the pro forma compensation cost for 1998 relating to the FMC Plan. The pro forma compensation cost relating to options still outstanding at December 31, 1998 was $ 348 for the period ending December 31, 1998. This amount has been included in determining the total compensation benefit for the FMC Plan for 1998.

1) except note 19 (p. 65 - p. 73)

19. Commitments and Contingencies

Contingent non-NMC liabilities of Fresenius Medical Care Holdings, Inc.

In connection with the Merger, Grace Chemicals, the non-healthcare business of W.R. Grace which was spun off prior to the Merger, has agreed to indemnify the Company and NMC against all liabilities of the Company and its successors, whether relating to events occurring before or after the Merger, other than liabilities arising from or relating to NMC operations. After the Merger the Company will remain contingently liable for certain liabilities with respect to pre-Merger matters that are not related to NMC operations. The Company believes that in view of the nature of the non-NMC liabilities and the expected impact of the Merger on Grace Chemicals' financial position, the risk of significant loss from non-NMC liabilities is remote.

Were events to violate the tax-free nature of the Merger, the resulting tax liability would be the obligation of the Company. Grace Chemicals has agreed to indemnify the Company for such a tax liability, subject to certain representations by Grace Chemicals, the Company, and Fresenius AG. If the Company was not able to collect on the indemnity, the tax liability would have a material adverse effect on the Company's business, the financial condition of the Company and the results of operations.

Legal proceedings and government investigations

OIG investigative subpoenas

In October 1995, NMC received five investigative subpoenas from the Office of the Inspector General ("OIG") of the Department of Health and Human Services. The subpoenas were issued in connection with an investigation being conducted by the OIG, the U.S. Attorney for the District of Massachusetts and others concerning possible violations of federal laws, including the anti-kickback statutes and the False Claims Act (the "OIG Investigation"). The subpoenas call for extensive document production relating to various aspects of NMC's business.

In connection with the OIG Investigation, FMCH continues to receive additional subpoenas directed to NMC or FMCH to obtain supplemental information and documents regarding the above-noted issues, or to clarify the scope of the original subpoenas.

The Company is cooperating with the OIG Investigation. The Company believes that the government continues to review and evaluate the voluminous information the Company has provided. As indicated above, the government continues, from time to time, to seek supplementing and/or clarifying information from the Company. The Company understands that the government has utilized a grand jury to investigate these matters. The Company expects that this process will continue while the government completes its evaluation of the issues.

The OIG Investigation covers the following areas: (a) NMC's dialysis services business ("DSD"), principally relating to its Medical Director contracts and compensation; (b) NMC's treatment of credit balances resulting from overpayments received under the Medicare, Medicaid, CHAMPUS and other government and commercial payors, its billing for home dialysis services, and its payment of supplemental medical insurance premiums on behalf of indigent patients; (c) NMC's LifeChem laboratory subsidiary's ("LifeChem") business, including testing procedures, marketing, customer relationships, competition, overpayments totaling approximately $ 4.9 million that were received by LifeChem from the Medicare program with respect to laboratory services rendered between 1989 and 1993, a 1997 review of dialysis clinics' standing orders, and the provision of discounts on products from NMC's products division, grants, equipment and entertainment to customers; and (d) NMC's homecare division ("Homecare") and, in particular, information concerning intradialytic parenteral nutrition ("IDPN") utilization, documentation of claims and billing practices including various services, equipment and supplies and payments made to third parties as compensation for administering IDPN therapy.

The government has indicated that the areas identified above are not exclusive, and that it may pursue additional areas. As noted, the penalties applicable under the anti-kickback statutes, the U.S. Federal False Claims Act (the "False Claims Act") and other federal and state statutes and regulations applicable to NMC's business can be substantial. While NMC asserts that it is able to offer legal and/or factual defenses with respect to many of the areas the government has identified, it is expected that the government will assert that NMC has violated multiple statutory and regulatory provisions. Additionally, nine and possibly other qui tam actions alleging that NMC submitted false claims to the government have been filed

under seal by former or current NMC employees or other individuals who may have familiarity with one or more of the issues under investigation. As noted, under the False Claims Act, any such private plaintiff could pursue an action against NMC in the name of the U.S. at his or her own expense if the government declines to do so. During the approximately three and one-half years since the initial subpoenas were served, NMC and the government have met periodically to discuss issues in connection with the OIG Investigation, including theories of liability. Recently, NMC and the government have begun to explore the possibility of settling the matters which are encompassed by the OIG Investigation and, as referenced below, have reached an agreement in principal in connection with the diagnostics investigation matter. There can be no assurance that any of the other matters subject to the OIG Investigation will be settled. If however, one or more of the matters encompassed by the OIG Investigation is settled, it may result in NMC acknowledging that its past practices violated federal statutes, as well as NMC incurring substantial civil and criminal financial penalties which could have a material adverse effect on the Company. If one or more of these matters is not settled, the government may be expected to initiate litigation in which it would seek substantial civil and criminal financial penalties and other sanctions that could result in the exclusion of NMC and its subsidiaries from the Medicare program, Medicaid program and other federal health care programs.

Diagnostics subpoena

In October 1996, Biotrax International, Inc. ("Biotrax") and NMC Diagnostics, Inc., ("DSI") both of which are subsidiaries of NMC, received an investigative subpoena from the OIG. The subpoena calls for the production of extensive documents and was issued in connection with an investigation being conducted by the OIG in conjunction with the U.S. Attorney for the Eastern District of Pennsylvania concerning the possible submission of false or improper claims to, and their payment by, the Medicare program. The subpoena calls for the production of documents on corporate organization, business plans, document retention, personnel files, sales and marketing and Medicare billing issues relating to certain procedures offered by the prior owner of the Biotrax business before its assets were acquired by NMC in March 1994 and by DSI following the acquisition. The Company has reviewed the subpoena with its legal counsel and has made extensive document production in response to the subpoena. The Company and the government have been negotiating a resolution to this matter, and negotiations have progressed to the point of a possible settlement. The Company and the government have reached an agreement in principle in which, among other things, the government has agreed to release the Company from liability in this matter in exchange for a payment of approximately $ 16.5 million from the Company. The Company and the government are currently negotiating the terms of a settlement agreement. The agreement is not final. For this reason, the eventual outcome of this matter, its duration, and its effect, if any, on NMC or the Company cannot be predicted at this time. The Company divested Non-Renal Diagnostic business on June 26, 1998 (see Note 5).

Medical Director compensation

The government is investigating whether Dialysis Services compensation arrangements with its Medical Directors constitute payments to induce referrals, which would be illegal under the anti-kickback statutes, rather than payment for services rendered. Dialysis Services compensated the substantial majority of its Medical Directors on the basis of a percentage of the earnings of the dialysis center for which the Medical Director was responsible from the inception of NMC's predecessor in 1972 until January 1, 1995, the effective date of Stark II. Under the arrangements in effect prior to January 1, 1995, the compensation paid to Medical Directors was adjusted to include "add backs," which represented a portion of the profit earned by NMC's Medical Products Group ("MPG") on products purchased by the Medical Director's facility from MPG and (until January 1, 1992) a portion of the profit earned by LifeChem on laboratory services provided to patients at the Medical Director's facility. These adjustments were designed to allocate a profit factor to each dialysis center relating to the profits that could have been realized by the center if it had provided the items and services directly rather than through a subsidiary of NMC. The percentage of profits paid to any specific Medical Director was reached through negotiation, and was typically a provision of a multi-year consulting agreement.

To comply with provisions of OBRA 93 (as hereafter defined) known as "Stark II" if Designated Health Services (as defined in Stark II) are involved, Medical Director compensation must not exceed fair market value and may not take into account the volume or value of referrals or other business generated between the parties. Since January 1, 1995, Dialysis Services has compensated its Medical Directors on a fixed compensation arrangement intended to comply with the requirements of Stark II. In renegotiating its Medical Director compensation arrangements in connection with Stark II, Dialysis Services took into and continues to take into account the compensation levels paid to its Medical Directors in prior years.

Certain government representatives have expressed the view in meetings with counsel for NMC that arrangements where the Medical Director was or is paid amounts in excess of the "fair market value" of the services rendered may evidence illegal payments to induce referrals, and that hourly compensation is a relevant measure for evaluating the "fair market value" of the services. Dialysis Services does not compensate its Medical Directors on an hourly basis and has asserted to the government that hourly compensation is not a determinative measure of fair market value. Although the Company believes that the compensation paid to its Medical Directors is generally reflective of fair market value, there can be no assurances that the government will agree with this position or that the Company ultimately will be able to defend its position successfully. Because of the wide variation in local market factors and in the profit percentage contractually negotiated between Dialysis Services and its Medical Directors prior to January 1, 1995, there is a wide variation in the amounts that have been paid to Medical Directors. As a result, the compensation that Dialysis Services has paid and is continuing to pay to a material number of its Medical Directors could be viewed by the government as being in excess of "fair market value," both in absolute terms and in terms of hourly compensation. NMC has asserted to the government that its compensation arrangements do not constitute illegal payments to induce referrals. NMC has also asserted to the government that OIG auditors repeatedly

reviewed NMC's compensation arrangements with its Medical Directors in connection with their audits of the costs claimed by Dialysis Services that the OIG stated in its audit reports that, with the exception of certain technical issues, NMC had complied with applicable Medicare laws and regulations pertaining to the end-stage renal disease ("ESRD") program; and that NMC reasonably relied on these audit reports in concluding that its program for compensating Medical Directors was lawful. There has been no indication that the government will accept NMC's assertions concerning the legality of its arrangements generally or NMC's assertion that it reasonably relied on OIG audits, or that the government will not focus on specific arrangements that Dialysis Services has made with one or more Medical Directors and assert that those specific arrangements were or are unlawful.

The government is also investigating whether Dialysis Services profit sharing arrangements with its Medical Directors influenced them to order unnecessary ancillary services and items. NMC has asserted to the government that the rate of utilization of ancillary services and items by its Medical Directors is reasonable and that it did not provide illegal inducements to Medical Directors to order ancillary services and items.

Credit balances

In the ordinary course of business, medical service providers like Dialysis Services receive overpayments from Medicare intermediaries and other payors for services that they provide to patients. Medicare intermediaries commonly direct such providers to notify them of the overpayment and not remit such amounts to the intermediary by check or otherwise unless specifically requested to do so. In 1992, the Health Care Financing Administration ("HCFA") adopted a regulation requiring certain Medicare providers, including dialysis centers, to file a quarterly form listing unrecouped overpayments with the Medicare intermediary responsible for reimbursing the provider. The first such filing was required to be made as of June 30, 1992 for the period beginning with the initial date that the provider participated in the Medicare program and ending on June 30, 1992.

The government is investigating whether Dialysis Services intentionally understated the Medicare credit balance reflected on its books and records for the period ending June 30, 1992 by reversing entries out of its credit balance account and taking overpayments into income in anticipation of the institution of the new filing requirement. Dialysis Services policy was to notify Medicare intermediaries in writing of overpayments upon receipt and to maintain unrecouped Medicare overpayments as credit balances on the books and records of DSD for four years; overpayments not recouped by Medicare within four years would be reversed from the credit balance account and would be available to be taken into income. NMC asserts that Medicare overpayments that have not been recouped by Medicare within four years are not subject to recovery under applicable regulations and that its initial filing with the intermediaries disclosed the credit balance on the books and records of Dialysis Services as shown in accordance with its policy, but there can be no assurance that the government will accept NMC's views. The government has inquired whether other divisions including Homecare, LifeChem and DSI have appropriately treated Medicare credit balances as well as credit balances of other payors.

The government is also investigating whether Dialysis Services failed to disclose Medicare overpayments that resulted from Dialysis Services' obligation to rebill commercial payors for amounts originally billed to Medicare under HCFA's initial implementation of the Omnibus Budget Reconciliation Act of 1993 ("OBRA 93") amendments to the secondary payor provisions of the Medicare Act. Dialysis Service experienced delays in reporting a material amount of overpayments after the implementation of the OBRA 93 amendments. NMC asserts that most of these delays were the result of the substantial administrative burdens placed on Dialysis Services as a consequence of the changing and inconsistent instructions issued by HCFA with respect to the OBRA 93 amendments and were not intentional. Substantially all overpayments resulting from the rebilling effort associated with the OBRA 93 amendments have now been reported. Procedures are in place that are designed to ensure that subsequent overpayments resulting from the OBRA 93 amendments will be reported on a timely basis.

Supplemental medical insurance

Dialysis Services provided grants or loans for the payment of premiums for supplemental medical insurance (under which Medicare Part B coverage is provided) on behalf of a small percentage of its patients who are financially needy. The practice of providing loans or grants for the payment of supplemental medical insurance premiums by NMC was one of the subjects of review by the government as part of the OIG Investigation.

The Government, however, advised the Company orally that it is no longer pursuing this issue. Furthermore, as a result of the passage of HIPAA, the Company terminated making such payments on behalf of its patients. Instead, the Company, together with other representatives of the industry, obtained an advisory opinion from the OIG, whereby, consistent with specified conditions, the Company and other similarly situated providers may make contributions to a non-profit organization that has volunteered to make these payments on behalf of indigent ESRD patients, including patients of the Company. In addition, the government has indicated that it is investigating the method by which NMC made Medigap payments on behalf of its indigent patients.

Overpayments for home dialysis services

NMC acquired Home Intensive Care, Inc. ("HIC"), an in-center and home dialysis service provider, in 1993. At the time of the acquisition, HIC was the subject of a claim by HCFA that HIC had received payments for home dialysis services in excess of the Medicare reasonable charge for services rendered prior to February 1, 1990. NMC settled the HCFA claim against HIC in 1994. The government is investigating whether the settlement concerning the alleged overpayments made to HIC resolved all issues relating to such alleged overpayments. The government is also investigating whether an NMC subsidiary, Home Dialysis Services, Inc. ("HDS"), received payments similar to the payments that HIC received, and whether HDS improperly billed for home dialysis services in excess of the monthly cost cap for services rendered on or after February 1, 1990. The government is investigating whether NMC was overpaid for services rendered. NMC asserts that the billings by HDS were proper, but there can be no assurance that the government will accept NMC's view.

LifeChem

Overpayments. On September 22, 1995, LifeChem voluntarily disclosed certain billing problems to the government that had resulted in LifeChem's receipt of approximately $4.9 million in overpayments from the Medicare program for laboratory services rendered between 1989 and 1993. LifeChem asserts that most of these overpayments relate to errors caused by a change in LifeChem's computer systems and that the remainder of the overpayments were the result of the incorrect practice of billing for a complete blood count with differential when only a complete blood count was ordered and performed, and of the incorrect practice of billing for a complete blood count when only a hemoglobin or hematocrit test was ordered. LifeChem asserts that the overpayments it received were not caused by fraudulent activity, but there can be no assurance that the government will accept LifeChem's view. LifeChem made these disclosures to the government as part of an application to be admitted to a voluntary disclosure program begun by the government in mid-1995. At the time of the disclosures, LifeChem tendered repayment to the government of the $4.9 million in overpayments. After the OIG Investigation was announced, the government indicated that LifeChem had not been accepted into its voluntary disclosure program. The government has deposited the $4.9 million check with NMC's approval. The matters disclosed in LifeChem's September 22, 1995 voluntary disclosure are a subject of the OIG Investigation.

On June 7, 1996, LifeChem voluntarily disclosed an additional billing problem to the government that had resulted in LifeChem's receipt of between $40,000 and $160,000 in overpayments for laboratory services rendered in 1991. LifeChem advised the government that this overpayment resulted from the submission for payment of a computer billing tape that had not been subjected to a "billing rules" program designed to eliminate requests for payments for laboratory tests that are included in the Composite Rate and that were not eligible for separate reimbursement. LifeChem also advised the government that there may have been additional instances during the period from 1990 to 1992 when other overpayments were received as a result of the submission of computer billing tapes containing similar errors and that it was in the process of determining whether such additional overpayments were received. On June 21, 1996, LifeChem advised the government that the 1991 billing problem disclosed on June 7, 1996 resulted in an overpayment of approximately $112,000. LifeChem also advised the government that certain records suggested instances in July 1990 and August 31 through September 11, 1990, when billing tapes may have been processed without rules processing. LifeChem continued its effort to determine whether any other overpayments occurred relating to the "billing rules" problem and, in March 1997, advised the government that an additional overpayment of approximately $260,000 was made by Medicare.

Capitation for routine tests and panel design. In October 1994, the OIG issued a special fraud alert in which it stated its view that the industry practice of offering to perform or performing the routine tests covered by the composite rate payment method (the "Composite Rate") at a price below fair market value, coupled with an agreement by a dialysis center to refer all or most of its non-Composite Rate tests to the laboratory, violates the anti-kickback statutes. In response to this alert, LifeChem changed its practices with respect to testing covered by the Composite Rate to increase the amount charged to both Dialysis Services and third-party dialysis centers and reduce the number of tests provided for the fixed rate. The government is investigating LifeChem's practices with respect to these tests.

Benefits provided to dialysis centers and persons associated with dialysis centers. The government is investigating whether Dialysis Services or any third-party dialysis center or any person associated with any such center was provided with benefits in order to induce them to use LifeChem services. Such benefits could include, for example, discounts on products or supplies, the provision of computer equipment, the provision of money for the purchase of computer equipment, the provision of research grants and the provision of entertainment to customers. NMC has identified certain instances in which benefits were provided to customers who purchased medical products from NMC Medical Products, Inc., NMC's products company, and used LifeChem's laboratory services. The government may assert that the provision of such benefits violates, among other things, the anti-kickback statutes. In December 1998, the former Vice President of Sales responsible for NMC's laboratory and products divisions pleaded guilty to the payment of illegal kickbacks to obtain laboratory business for NMC. In February 1999, the former President of NMC Medical Products, Inc. was indicted by the government for the payment of these same and/or similar kickbacks.

Business and testing practices. As noted above, the government has identified a number of specific categories of documents that it is requiring NMC to produce in connection with LifeChem business and testing practices. In addition to documents relating to the areas discussed above, the government has also required LifeChem to produce documents relating to the equipment and systems used by LifeChem in performing and billing for clinical laboratory blood tests, the design of the test panels offered and requisition forms used by LifeChem, the utilization rate for certain tests performed by LifeChem, recommendations concerning diagnostic codes to be used in ordering tests for patients with given illnesses or conditions, internal and external audits and investigations relating to LifeChem's billing and testing. Subsequently, the government served an investigative subpoena for documents concerning the Company's 1997 review of dialysis clinics' standing orders, and responsive documents were provided. Recently the government served investigative subpoenas requiring NMC to update its production on the above issues and to produce contract files for twenty-three identified dialysis clinic customers. The government is investigating each of these areas, and asserts that LifeChem and/or NMC have violated the False Claims Act and/or the Anti-Kickback Statute through the test ordering, paneling, requisitioning, utilization, coding, billing and auditing practices described above.

Intradialytic parenteral nutrition

Administration kits. One of the activities of SRM is to provide IDPN therapy to dialysis patients at both NMC-owned facilities and at facilities owned by other providers. IDPN therapy was provided by Homecare prior to its divestiture. IDPN therapy is typically provided

to the patient 12-13 times per month during dialysis treatment. Bills are submitted to Medicare on a monthly basis and include separate claims for reimbursement for supplies, including, among other things, nutritional solutions, administration kits and infusion pumps. In February 1991, the Medicare carrier responsible for processing Homecare's IDPN claims issued a Medicare advisory to all parenteral and enteral nutrition suppliers announcing a coding change for reimbursement of administration kits provided in connection with IDPN therapy for claims filed for items provided on or after April 1, 1991. The Medicare allowance for administration kits during this period was approximately $625 per month per patient. The advisory stated that IDPN providers were to indicate the "total number of actual days" when administration kits were "used," instead of indicating that a one-month supply of administration kits had been provided. In response, Homecare billed for administration kits on the basis of the number of days that the patient was on an IDPN treatment program during the billing period, which typically represented the entire month, as opposed to the number of days the treatment was actually administered. During the period from April 1991 to June 1992, Homecare had an average of approximately 1,200 IDPN patients on service.

In May 1992, the carrier issued another Medicare advisory to all PEN suppliers in which it stated that it had come to the carrier's attention that some IDPN suppliers had not been prorating their billing for administration kits used by IDPN patients and that providers should not bill for administration kits on the basis of the number of days that the patient was on an IDPN treatment program during the billing period. The advisory stated further that the carrier would be conducting "a special study to determine whether or not overpayments have occurred as a result of incorrect billing" and that "if overpayments have resulted, providers that have incorrectly billed" would "be contacted so that refunds can be recovered." Homecare revised its billing practices in response to this advisory for claims filed for items provided on or after July 1, 1992. Homecare was not asked to refund any amounts relating to its billings for administration kits following the issuance of the second advisory. The government asserts that NMC submitted false claims for administration kits during the period from 1988 to June 30, 1996, and that Homecare's billing for administration kits during this period violated, among other things, the False Claims Act.

Infusion pumps and IV poles. During the time period covered by the subpoenas, Medicare regulations permitted IDPN providers to bill Medicare for the infusion pumps and, until 1992, for IV poles provided to IDPN patients in connection with the administration of IDPN treatments. These regulations do not expressly specify that a particular pump and IV pole be dedicated to a specific patient, and NMC asserts that these regulations permitted Homecare to bill Medicare for an infusion pump and IV pole so long as the patient was infused using a pump and IV pole. Despite the absence of an express regulatory specification, Homecare developed a policy to deliver to a dialysis center a dedicated infusion pump and IV pole for each patient, although the Company cannot represent that Homecare followed this policy in every instance. The government is investigating the propriety of Homecare's billings for infusion pumps and IV poles and asserts that Homecare's billings violate the False Claims Act.

As noted above, under the new policies published by HCFA with respect to IDPN therapy, the Company has not been able to bill for infusion pumps after July 1, 1996. The government discontinued reimbursement for IV poles in 1992.

"Hang fees" and other payments. IDPN therapy is typically provided to the patient during dialysis by personnel employed by the dialysis center treating the patient with supplies provided and billed to Medicare by Homecare in accordance with the Medicare parenteral nutrition supplier rules. In order to compensate dialysis centers for the costs incurred in administering IDPN therapy and monitoring the patient during therapy, Homecare followed the practice common in the industry of paying a "hang fee" to the center. Dialysis centers are responsible for reporting such fees to HCFA on their cost reports. For Dialysis Services dialysis centers, the fee was $30 per administration, based upon internal Dialysis Services cost calculations. For third-party dialysis centers, the fee was negotiated with each center, typically pursuant to a written contract, and ranged from $15 to $65 per administration. The Company has identified instances in which other payments and amounts beyond that reflected in a contract were paid to these third-party centers. The Company has stopped paying "hang fees" to both Dialysis Services and third-party facilities.

In July 1993, the OIG issued a management advisory alert to HCFA in which it stated that "hang fees" and other payments made by suppliers of IDPN to dialysis centers "appear to be illegal as well as unreasonably high." The government is investigating the nature and extent of the "hang fees" and other payments made by Homecare as well as payments by Homecare to physicians whose patients have received IDPN therapy. The government may assert that the payments by Homecare to dialysis centers violate, among other things, the anti-kickback statutes.

Utilization of IDPN. Since 1984, when HCFA determined that Medicare should cover IDPN and other parenteral nutrition therapies, the Company has been an industry leader in identifying situations in which IDPN therapy is beneficial to ESRD patients. It is the policy of the Company to seek Medicare reimbursement for IDPN therapy only when it is prescribed by a patient's treating physician and when it believes that the circumstances satisfy the requirements published by HCFA and its carrier agents. Prior to 1994, HCFA and its carriers approved for payment more than 90% of the IDPN claims submitted by Homecare. After 1993, the rate of approval for Medicare reimbursement for IDPN claims submitted by Homecare for new patients and by the infusion industry in general, fell to approximately 9%. The Company contends that the reduction in rates of approval occurred because HCFA and its carriers implemented an unauthorized change in coverage policy without giving notice to providers. While NMC continued to offer IDPN to patients pursuant to the prescription of the patients' treating physicians and to submit claims for Medicare reimbursement when it believed the requirements stated in HCFA's published regulations were satisfied, other providers responded to the drop in the approval rate for new Medicare IDPN patients by abandoning the Medicare IDPN business, cutting back on the number of Medicare patients to whom they provide IDPN, or declining to add new Medicare patients. Beginning in 1994 the number of patients to whom NMC provided IDPN increased as a result.

The government is investigating the utilization rate of IDPN therapy among NMC patients, whether NMC submitted IDPN claims to Medicare for patients who were not eligible for coverage, and whether documentation of eligibility was adequate. NMC asserts that the utilization rate of IDPN therapy among its dialysis patients, which, in 1995, averaged less than 3.5 %, is the result of the factors discussed above and that it is the policy of Homecare to seek Medicare reimbursement for IDPN therapy prescribed by the patients' treating physician in accordance with the requirements published by HCFA and its carrier agents. There can be no assurance that the government will accept NMC's view. The government asserts that Homecare submitted IDPN claims for individuals who were not eligible for coverage and/or with inadequate documentation of eligibility.

The Company believes that it has presented to the government substantial defenses which support NMC's interpretation of coverage rules of IDPN as HCFA and its carriers published and explained them, and which demonstrated that HCFA and its carriers improperly implemented unpublished, more restrictive criteria after 1993. Nevertheless, the government is expected to assert in the OIG Investigation that, on a widespread basis, NMC submitted and received payments on claims for IDPN to Medicare for patients who were not eligible for coverage, and for whom the documentation of eligibility was inadequate.

In addition, the government asserts that, in a substantial number of cases, documentation of eligibility was false or inaccurate. With respect to some claims, the Company has determined that false or inaccurate documentation was submitted, deliberately or otherwise. The government continues to investigate the IDPN claims.

Qui tam actions

The Company and NMC have become aware that nine qui tam actions have been filed in various jurisdictions. Each of these actions is under seal and in each action, pursuant to court order the seal has been modified to permit the Company, FMCH, NMC and other affiliated defendants to disclose the complaint to any relevant investors, financial institutions and/or underwriters, their successors and assigns and their respective counsel and to disclose the allegations in the complaints in their respective U.S. Securities and Exchange Commission (the "SEC" or the "Commission") and New York Stock Exchange ("NYSE") periodically required filings.

The first qui tam action was filed in the United States District Court for the Southern District of Florida in 1996, amended on July 8, 1996 and disclosed to the Company on July 10, 1996. It alleges, among other things, that Grace Chemicals and NMC violated the False Claims Act in connection with certain billing practices regarding IDPN and the administration of EPO and that as a result of this allegedly wrongful conduct, the United States suffered actual damages in excess of $ 200 million. The Amended Complaint also seeks the imposition of a constructive trust for the benefit of the United States on the proceeds of the NMC dividend paid to Grace Chemicals in connection with the Merger on the ground that the Merger constituted a fraudulent conveyance that will render NMC unable to satisfy the claims asserted in the Amended Complaint.

The second qui tam action was filed in the United States District Court for the Middle District of Florida in 1995 and disclosed to the Company on or before November 7, 1996. It alleges, among other things, that NMC and certain NMC subsidiaries violated the False Claims Act in connection with the alleged retention of overpayments made under the Medicare program, the alleged submission of claims in violation of applicable cost caps and the payment of supplemental Medicare insurance premiums as an alleged inducement to patients to obtain dialysis products and services from NMC. The complaint alleges that as a result of this allegedly wrongful conduct, the United States suffered damages in excess of $ 10 million including applicable fines.

The third qui tam action was filed in the United States District Court for the Eastern District of Pennsylvania in February 1996 and was disclosed to the Company in November 1996. It alleges, among other things, that a pharmaceutical manufacturer, an unaffiliated dialysis provider and NMC violated the False Claims Act in connection with the submission of claims to the Medicare program for a nonsterile intravenous drug and for intravenous drugs which were allegedly billed in excess of permissible Medicare reimbursement rates. The complaint also asserts that the defendants violated the Medicare and Medicaid anti-kickback statutes in connection with the receipt of discounts and other in kind payments as alleged inducements to purchase intravenous drugs. The complaint is focused on the business relationship between the pharmaceutical manufacturer and several providers, one of which is NMC. The complaint asserts that as a result of this allegedly wrongful conduct, the United States suffered damages. On June 28, 1997, in response to relator's motion to dismiss and the United States' declination to intervene, the District Court ordered the complaint dismissed without prejudice.

The fourth qui tam action was filed in the United States District Court for the Eastern District of Pennsylvania in May 1995 and was disclosed to the Company in August 1997. It alleges, among other things, that Biotrax violated the False Claims Act in connection with its submission of claims to the Medicare program for diagnostic tests and induced overutilization of such tests in the medical community through improper marketing practices also in violation of the False Claims Act.

The fifth qui tam action was filed in the United States District Court for the Eastern District of Pennsylvania in August 1996 and was disclosed to the Company in August 1997. It alleges, among other things, that Biotrax and NMC Diagnostic Services induced overutilization of diagnostic tests by several named and unnamed physician defendants in the local medical community, through improper marketing practices and fee arrangements, in violation of the False Claims Act.

The sixth qui tam action was filed in the United States District Court for the Eastern District of Pennsylvania in November 1996 and was disclosed to the Company in August 1997. It alleges, among other things, that NMC, DSI and Biotrax violated the False Claims Act in connection with the submission of claims to the Medicare program by improperly upcoding and otherwise billing for various diagnostic tests.

The seventh qui tam action was filed in the United States District Court for the District of Delaware in January 1997 and was disclosed to the Company in September 1997. It alleges, among other things, that NMC and Biotrax violated the False Claims Act in connection with the submission of claims to the Medicare program for diagnostic

tests, and induced overutilization of such tests through improper marketing practices which provided impermissible incentives to health care providers to order these tests.

The eighth qui tam action was filed in the United States District Court for the District of New Jersey in February 1997 and was disclosed to the Company in September 1997. It alleges, among other things, that DSI and NMC violated the False Claims Act in connection with the submission of claims to the Medicare program for reimbursement for diagnostic tests, by causing unnamed physicians to overutilize these tests through a variety of fee arrangements and other impermissible inducements.

The ninth qui tam was filed in the United States District Court for the District of Massachusetts in 1994 and was disclosed to the Company in February 1999. It alleges among other things that NMC violated the False Claims Act and the Anti-Kickback Statute in connection with certain billing and documentation practices regarding IDPN therapy, home oxygen therapy and certain medical billings in NMC's Chicago office.

Each of the qui tam complaints asserts that as a result of the allegedly wrongful conduct, the United States suffered damages and that the defendants are liable to the United States for three times the amount of the alleged damages plus civil penalties of up to $ 10,000 per false claim. An adverse result in any of the qui tam actions could have a material adverse affect on the Company's business, financial condition or results of operations.

OIG Agreements

As a result of discussions with representatives of the United States in connection with the OIG Investigation, certain agreements (the "OIG Agreements") have been entered into to guarantee the payment of any obligations of NMC to the United States (an "Obligation") relating to or arising out of the OIG Investigation and the qui tam action filed in the Southern District of Florida (the "Government Claims"). For the purposes of the OIG Agreements, an Obligation is (a) a liability or obligation of NMC to the United States in respect of a Government Claim pursuant to a court order (i) which is final and nonappealable or (ii) the enforcement of which has not been stayed pending appeal or (b) a liability or obligation agreed to be an Obligation in a settlement agreement executed by the Company, FMCH, or NMC, on the one hand, and the United States, on the other hand. As stated elsewhere herein, the outcome of the OIG Investigation cannot be predicted.

Pursuant to the OIG Agreements, upon consummation of the Merger, the Company, FMCH, and NMC provided the United States with a joint and several unconditional guarantee of payment when due of all Obligations (the "Primary Guarantee"). As credit support for this guarantee, NMC delivered an irrevocable standby letter of credit in the amount of $ 150 million. The United States will return such letter of credit (or any renewal or replacement) for cancellation when all Obligations have been paid in full or it is determined that NMC has no liability in respect of the Government Claims. Under the terms of the Merger, any potential resulting monetary liability has been retained by NMC, and the Company and FMCH have indemnified Grace Chemicals against all potential liability arising from or relating to the OIG Investigation.

FMC and the United States state in the OIG Agreements that they will negotiate in good faith to attempt to arrive at a consensual resolution of the Government Claims and, in the context of such negotiations, will negotiate in good faith as to the need for any restructuring of the payment of any Obligations arising under such resolution, taking into account the ability of FMC to pay the Obligations. The OIG Agreements state that the foregoing statements shall not be construed to obligate any person to enter into any settlement of the Government Claims or to agree to a structured settlement. Moreover, the OIG Agreements state that the statements described in the first sentence of this paragraph are precatory and statements of intent only and that (a) compliance by the United States with such provisions is not a condition or defense to the obligations of FMC under the OIG Agreements and (b) breach of such provisions by the United States cannot and will not be raised by FMC to excuse performance under the OIG Agreements. Neither the entering into of the OIG Agreements nor the providing of the Primary Guarantee and the $ 150 million letter of credit is an admission of liability by any party with respect to the OIG Investigation, nor does it indicate the liability, if any, which may result therefrom.

The foregoing describes the material terms of the OIG Agreements, copies of which were previously filed with the Commission and copies of which may be examined without charge at the public reference facilities maintained by the Commission at Room 1024, 450 Fifth Street, N.W. Washington, D.C. 20549, and at the Regional Offices of the Commission located at Suite 1400, Citicorp Center, 500 West Madison Street, Chicago, Illinois 60661-2551 and Room 1300, 7 World Trade Center, New York, New York 10048. Copies of such material will also be made available by mail from the Public Reference Branch of the Commission at 450 Fifth Street, N.W. Washington, D.C. 20549, at prescribed rates. The foregoing description does not purport to be complete and is qualified in its entirety by reference to such agreements.

An adverse determination with respect to any of the issues addressed by the subpoenas, or any of the other issues that have been or may be identified by the government, could result in the payment of substantial fines, penalties and forfeitures, the suspension of payments or exclusion of the Company or one or more of its subsidiaries from the Medicare program and other federal programs, and changes in billing and other practices that could adversely affect the Company's revenues. Any such result could have a material adverse effect on the Company's business, financial condition and results of operations.

Omnibus Budget Reconciliation Act of 1993. OBRA 93 affected the payment of benefits under Medicare and employer health plans for certain dual eligible ESRD patients. In July 1994, HCFA issued an instruction to Medicare claims processors to the effect that Medicare benefits for the patients affected by OBRA 93 would be subject to a new 18-month "coordination of benefits" period. This instruction had a positive impact on NMC's dialysis revenues because, during the 18-month coordination of benefits period, patients' employer health plans were responsible for payment, which was generally at rates higher than that provided under Medicare.

In April 1995, HCFA issued a new instruction, reversing its original instruction in a manner that would substantially diminish the positive effect of the original instruction on NMC's dialysis business.

HCFA further proposed that its new instruction be effective retroactive to August 1993, the effective date of OBRA 93.
NMC ceased to recognize the incremental revenue realized under the original Program Memorandum as of July 1, 1995, but it continued to bill employer health plans as primary payors for patients affected by OBRA 93 through December 31, 1995. As of January 1, 1996, NMC commenced billing Medicare as primary payor for dual eligible ESRD patients affected by OBRA 93, and then began to rebill in compliance with the revised policy for services rendered between April 24 and December 31, 1995.
On May 5, 1995, NMC filed a complaint in the U.S. District Court for the District of Columbia (National Medical Care, Inc. and Bio-Medical Applications of Colorado, Inc. d/b/a Northern Colorado Kidney Center v. Shalala, C.A. No. 95-0860 (WBB)) seeking to preclude HCFA from retroactively enforcing its April 24, 1995 implementation of the OBRA 93 provisions relating to the coordination of benefits for dual eligible ESRD patients. On May 9, 1995, NMC moved for a preliminary injunction to preclude HCFA from enforcing its new policy retroactively, that is, to billings for services provided between August 10, 1993 and April 23, 1995. On June 6, 1995, the court granted NMC's request for a preliminary injunction and in December of 1996, NMC moved for partial summary judgment seeking a declaration from the Court that HCFA's retroactive application of the April 1995 rule was legally invalid. HCFA cross-moved for summary judgment on the grounds that the April 1995 rule was validly applied prospectively.
In January 1998, the court granted NMC's motion for partial summary judgment and entered a declaratory judgment in favor of NMC, holding HCFA's retroactive application of the April 1995 rule legally invalid, and based on its finding, the Court also permanently enjoined HCFA from enforcing and applying the April 1995 rule retroactively against NMC. The Court took no action on HCFA's motion for summary judgment pending completion of outstanding discovery.
On October 5, 1998 NMC filed it's own motion for summary judgment requesting that the Court declare HCFA's prospective application of the April 1995 rule invalid and permanently enjoin HCFA from prospectively enforcing and applying the April 1995 rule. The Court has not yet ruled on the parties' motions. HCFA elected not to appeal from the Court's June 1995 and January 1998 orders. HCFA may, however, appeal all rulings at the conclusion of the litigation.
If HCFA should successfully appeal so that the revised interpretation would be applied retroactively NMC may be required to refund the payments received from employer health plans for services provided after August 10, 1993 under HCFA's original implementation, and to re-bill Medicare for the same services, which would result in a net loss to Dialysis Services of approximately $120 million attributable to all periods prior to December 31, 1995. Also, in such event, the Company's business, financial position and results of operations would be materially adversely affected.

Intradialytic parenteral nutrition coverage issues.
SRM administers IDPN therapy to chronic dialysis patients who suffer from severe gastrointestinal malfunctions. IDPN therapy was provided by Homecare prior to its divestiture. After 1993, Medicare claims processors sharply reduced the number of IDPN claims approved for payment as compared to prior periods. NMC believes that the reduction in IDPN claims represented an unauthorized policy coverage change. Accordingly, NMC and other IDPN providers pursued various administrative and legal remedies, including administrative appeals, to address this reduction.
In November 1995, NMC filed a complaint in the U.S. District Court for the Middle District of Pennsylvania seeking a declaratory judgment and injunctive relief to prevent the implementation of this policy coverage change. (National Medical Care, Inc. v. Shalala, 3:CV-95-1922 (RPC)). Subsequently, the District Court affirmed a prior report of the magistrate judge dismissing NMC's complaint, without considering any substantive claims, on the grounds that the underlying cause of action should be submitted fully to the administrative review processes available under the Medicare Act. NMC decided not to appeal the Court's decision, but rather, to pursue the claims through the available administrative processes.
NMC was successful in pursuing these claims through the administrative process, receiving favorable decisions from Administrative Law Judges in more than 80% of its cases. In early 1998, a group of claims which had been ruled on favorably were remanded by the Medical Appeals Council to a single Administrative Law Judge (the "ALJ") with extensive instructions concerning the review of these decisions. A hearing was scheduled on the remanded claims to take place in July, but later postponed until October 1998.
Prior to the July hearing date, the United States Attorney for the District of Massachusetts requested that the hearing be stayed pending resolution of the OIG Investigation, on the basis that the proceeding could adversely effect the government's investigation as well as the government's efforts to confirm its belief that these claims are false. Prior to the ALJ issuing a decision on the stay request, the U.S. Attorney's Office requested that NMC agree to a stay in the proceedings in order to achieve a potential resolution of the IDPN claims subject to the OIG Investigation as well as those which are subject to the administrative appeals process. NMC has agreed to this request, and together with the U.S. Attorney's Office has requested a stay. The ALJ has agreed to this request in order to allow the parties the opportunity to resolve both the IDPN claims which are the subject of the OIG Investigation and the IDPN claims which are the subject of the administrative proceedings. At this time, it is not possible to determine whether NMC and the government will be able to resolve issues surrounding the IDPN claims. Further proceedings on all other government appeals from the Administrative Law Judges' decisions favorable to the Company have also been stayed by agreement of the parties.
Although NMC management believes that those IDPN claims were consistent with published Medicare coverage guidelines and ultimately will be approved for payment, there can be no assurance that the claims on appeal will be approved for payment. Such claims represent substantial accounts receivable of NMC, amounting to approximately $150 million as of December 31, 1998.
If NMC is unable to collect its IDPN receivable, either through the administrative appeal process or through negotiation, or if IDPN coverage is reduced or eliminated, depending on the amount of the receivable that is not collected and/or the nature of the coverage change, the Company's business, financial condition and results of operations could be materially adversely affected. NMC's IDPN receivables are included in the net assets of the Company's discontinued operations. However, these receivables have not been

sold and will remain classified as discontinued operations until they have been settled. See Notes to Consolidated Financial Statements Note 5.

Other legal proceedings

District of New Jersey investigation

NMC has received multiple subpoenas from a federal grand jury in the District of New Jersey investigating, among other things, whether NMC sold defective products, the manner in which NMC handled customer complaints and certain matters relating to the development of a new dialyzer product line. NMC is cooperating with this investigation and has provided the grand jury with extensive documents. In February, 1996, NMC received a letter from the U.S. Attorney for the District of New Jersey indicating that it is the target of a federal grand jury investigation into possible violations of criminal law in connection with its efforts to persuade the FDA to lift a January 1991 import hold issued with respect to NMC's Dublin, Ireland manufacturing facility. In June 1996, NMC received a letter from the U.S. Attorney for the District of New Jersey indicating that the U.S. Attorney had declined to prosecute NMC with respect to a submission related to NMC's effort to lift the import hold. The letter added that NMC remains a subject of a federal grand jury's investigation into other matters. NMC has produced documents in response to a June 1996 subpoena from the federal grand jury requesting certain documents in connection with NMC's imports of the FOCUS® dialyzer from January 1991 to November 1995. The government investigators and the Company have narrowed the issues with respect to which the government has previously expressed concerns and recently have conducted discussions in order to resolve this investigation. However, the outcome and impact, if any, of these discussions and potential resolution on the Company's business, financial condition or results of operations cannot be predicted at this time.

Commercial insurer litigation

In 1997, FMCH, NMC and certain named NMC subsidiaries, were served with a civil complaint filed by Aetna Life Insurance Company in the U.S. District Court for the Southern District of New York (Aetna Life Insurance Company v. National Medical Care, Inc. et al, 97-Civ-9310). Based in large part on information contained in prior securities filings, the lawsuit alleges inappropriate billing practices for nutritional therapy, diagnostic and clinical laboratory tests and misrepresentations. The complaint seeks unspecified damages and costs. This matter is at a relatively early stage in the litigation process, with substantial discovery just beginning and its outcome and impact on the Company cannot be predicted at this time. However, the Company, NMC and its subsidiaries believe that they have substantial defenses to the claims asserted, and intend to continue to vigorously defend the lawsuit. It is also possible that one or more other private payors may assert that NMC received excess payments and similarly, may seek reimbursement and other damages from NMC. An adverse result could have a material adverse effect on the Company's business, financial condition or results of operations.

Administrative appeals

The Company regularly pursues various administrative appeals relating to reimbursement issues in connection with its dialysis clinics. One such appeal consists of a challenge to the Medicare regulation which capped reimbursement for the bad debts incurred by dialysis clinics. In 1998, the United States Court of Appeals for the District of Columbia ruled in favor of the Company in connection with the bad debt issue, holding that the Secretary of Health and Human Services had not adequately justified the bad debt regulation, and ruling that the government's order adopting the rule was arbitrary and capricious. The Court of Appeals remanded the matter to the Secretary to provide a more adequate explanation of the bad debt cap or to abandon it. Subsequently, the Court modified its holding to continue the bad debt regulation in effect pending remand. The Company has recently begun settlement discussions with the government in an attempt to recover reimbursement for disallowed bad debt expenses. The Company cannot predict the outcome of these discussions.

20. Financial Intruments

Market risk

The Company is exposed to market risk from changes in interest rates and foreign exchange rates. In order to manage the risk of interest rate and currency exchange rate fluctuations, the Company enters into various hedging transactions with investment grade financial institutions as authorized by the Company's Managing Board. The Company does not use financial instruments for trading purposes.

Foreign exchange risk management

The Company conducts business on a global basis in several major international currencies. As such, it is exposed to movements in foreign currency exchange rates. The Company enters into forward foreign exchange contracts to reduce certain currency exposures. At the present time, the Company hedges only those currency exposures associated with certain nonfunctional currency assets and liabilities.

Gains and losses on the contracts are included in other income and offset foreign exchange gains or losses from the revaluation of intercompany balances or other current assets and liabilities denominated in currencies other than the functional currency of the reporting entity. The Company's forward currency contracts generally range from 1 to 24 months in original maturity. Forward exchange contracts outstanding and their unrealized gains and losses as of December 31, 1998, which are recorded in other assets, are summarized as follows (in USD thousands):

	Contract Amount Sold	Contract Amount Purchased	Unrealized Gain/ (Loss)
Deutsche Mark	49,752	150,055	3,843
British Pound	6,496	29,042	910
Other currencies	7,987	44,265	(711)
	64,235	**223,362**	**4,042**

$ in thousands

The Company's forward exchange contracts contain credit risk in that its banking counterparties may be unable to meet the terms of the agreements. The potential risk of loss with any one party resulting from this type of credit risk is monitored. Management does not expect any material losses as a result of default by other parties.

Interest rate risk management

The Company enters into derivatives, particularly interest rate swaps, to protect interest rate exposures arising from long-term borrowings and accounts receivable securitization programs at floating rates by effectively swapping them into fixed rates that are lower than those available to the Company if fixed-rate borrowings were made directly. Under interest rate swaps, the Company agrees with other parties to exchange, at specified intervals, the difference between fixed-rate and floating-rate interest amounts calculated by reference to an agreed nominal principal amount.

The Company also enters into forward starting derivatives, including interest rate collar agreements to reduce the impact of changes in interest rates on its floating-rate long-term debt. No premiums were paid or received for the interest rate collar agreements.

The Company enters into various types of interest rate contracts in managing its interest rate risk, as indicated in the following table.

	1998		1997	
	Nominal Amount	Credit Exposure	Nominal Amount	Credit Exposure
Interest rate swaps	1,350,000	0	1,950,000	0
Forward starting interest rate derivatives	250,000	0	0	0

$ in thousands

The nominal amounts of derivatives do not represent amounts exchanged by the parties and, thus, are not a measure of exposure through its use of derivatives. The amounts exchanged are determined by reference to the nominal amounts and the other terms of the derivatives.

FMC is exposed to credit-related losses in the event of nonperformance by counterparties to financial instruments but does not expect any counterparties to fail to meet their obligations. The current credit exposure of derivatives is represented by the fair value of contracts with a positive fair value at the reporting date.

The Company had receive-variable/pay-fixed swaps with nominal amounts of $ 1,450,000 and $ 1,950,000 with average pay rates of 6.43 % and 6.26 % as of December 31, 1998 and 1997, respectively.

Fair value of financial instruments

The following table presents the carrying amounts and fair values of the Company's financial instruments at December 31, 1998 and 1997. FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, defines the fair value of a financial instrument as the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

	1998		1997	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Non-derivates				
Assets				
Cash and cash equivalents	31,867	31,867	37,818	37,818
Receivables	590,125	590,125	498,273	498,273
IDPN receivables	150,000	150,000	150,000	150,000
Liabilities				
Accounts and income taxes payable	299,774	299,774	262,825	262,825
Debt	1,127,011	1,127,011	1,657,570	1,657,570
Trust Preferred Securities	988,904	1,002,390	360,000	376,200
Derivatives				
Foreign exchange contracts	4,042	4,042	(2,113)	(2,113)
Swaps and interest rate collars	0	(51,541)	0	(23,448)

$ in thousands

The carrying amounts in the table are included in the statement of financial position under the indicated captions, except for derivative asset amounts, which are included in other assets.

Estimation of fair values

The following notes summarize the major methods and assumptions used in estimating the fair values of financial instruments.

Short-term financial instruments are valued at their carrying amounts included in the statement of financial position, which are reasonable estimates of fair value due to the relatively short period to maturity of the instruments. This approach applies to cash and cash equivalents, receivables, and accounts and income taxes payable.

Rates currently available to the Company for long-term borrowings with similar terms and remaining maturities are used to estimate the fair value of existing borrowings at the present value of expected cash flows.

The fair value of the Trust Preferred Securities is based upon market quotes.

The fair value of derivatives generally reflects the estimated amounts that the Company would receive or pay to terminate the contracts at the reporting date, thereby taking into account the current unrealized gains or losses of open contracts. Dealer quotes are available for most of the Company's derivatives.

21. Business Segment Information

During fiscal year 1998, Fresenius Medical Care AG reorganized its reporting structure to conform to the manner in which the Company is managed. FMC adopted SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*, in 1998. SFAS No. 131 established the standards for reporting information about operating segments in annual financial statements and requires selected information about operating segments in interim financial reports issued to stockholders. It also established standards for related disclosures about products and services, and geographic areas. Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance. FMC's chief operating decision maker is the Chief Executive Officer (CEO).

The Company has two reportable segments, North America and International, which were determined based upon how the Company manages its businesses. Both segments are primarily engaged in a) providing kidney dialysis and related services and performing related clinical laboratory testing and renal diagnostic services and b) manufacturing and distributing products and equipment for the treatment of end-stage renal disease. The accounting policies of the operating segments are the same as those described in Note 2.

Management evaluates the segments using a measure which reflects all of the segment's controllable revenues and expenses. The most appropriate measure in this regard is earnings before interest and

taxes (EBIT). In addition to EBIT, management believes that earnings before interest, taxes, depreciation and amortization (EBITDA) is helpful for investors as a measurement of the segment's and the Company's ability to generate cash and to service its financing obligations. EBITDA is also the basis for determining the compliance with certain covenants contained in the NMC credit agreement and indentures relating to the Trust Preferred Securities.
The Company's North American segment generates approximately 50 % of the Company's Dialysis Care revenue from sources subject to regulations under governmental programs. The company maintains reserves for losses related to their programs, including uncollectible accounts receivable, and such losses have been within management's expectations.
Information pertaining to the Company's two business segments is set forth below:

	North America	International	Corporate	Total
1998				
Net revenue external customers	2,562,603	943,073	–	3,505,676
Inter-segment revenue	2,159	43,476	(45,635)	–
Total net revenue	**2,564,762**	**986,549**	**(45,635)**	**3,505,676**
EBITDA	**548,986**	**227,789**	**(8,813)**	**767,962**
Depreciation and amortization	(214,940)	(62,362)	(1,682)	(278,984)
EBIT	**334,046**	**165,427**	**(10,495)**	**488,978**
Segment assets	4,630,168	961,972	87,279	5,679,419
Capital expenditures and acquisitions	244,788	177,886	761	423,435
1997				
Net revenue external customers	2,156,622	817,747	–	2,974,369
Inter-segment revenue	733	49,540	(50,273)	–
Total net revenue	**2,157,355**	**867,287**	**(50,273)**	**2,974,369**
EBITDA	**456,898**	**192,112**	**(7,686)**	**641,324**
Depreciation and amortization	(199,048)	(50,093)	(1,247)	(250,388)
EBIT	**257,850**	**142,019**	**(8,933)**	**390,936**
Segment assets	4,766,249	730,001	44,783	5,541,033
Capital expenditures and acquisitions	607,193	125,391	2,879	735,463
1996				
Net revenue external customers	775,689	643,846	–	1,419,535
Inter-segment revenue	1,706	47,481	(49,187)	
Total net revenue	**777,395**	**691,327**	**(49,187)**	**1,419,535**
EBITDA	**153,646**	**140,630**	**(1,796)**	**292,480**
Depreciation and amortization	(62,711)	(28,479)	–	(91,190)
EBIT	**90,935**	**112,151**	**(1,796)**	**201,290**
Capital expenditures and acquisitions	62,948	60,333	–	123,281

$ in thousands

	1998	1997	1996
Reconciliation of measures to consolidated totals			
Total EBITDA of reporting segments	776,775	649,010	294,276
Total depreciation and amortization	(278,984)	(250,388)	(91,190)
Corporate expenses	(8,813)	(7,686)	(1,796)
Interest expense	(228,182)	(193,860)	(61,475)
Interest income	8,641	10,312	4,887
Total income from continuing operations before income taxes, minority interest and cumulative effect of accounting change	**269,437**	**207,388**	**144,702**
Total EBIT of reporting segments	499,473	399,869	203,086
Corporate expenses	(10,495)	(8,933)	(1,796)
Interest expense	(228,182)	(193,860)	(61,475)
Interest income	8,641	10,312	4,887
Total income from continuing operations before income taxes, minority interest and cumulative effect of accounting change	**269,437**	**207,388**	**144,702**
Depreciation and amortization			
Total depreciation and amortization of reporting segments	277,302	249,141	91,190
Corporate depreciation and amortization	1,682	1,247	–
Total depreciation and amortization	**278,984**	**250,388**	**91,190**
Assets			
Total assets of reporting segments	5,592,140	5,496,250	
Corporate assets	87,279	44,783	
Total assets	**5,679,419**	**5,541,033**	

$ in thousands

For the geographic presentation, revenues are attributed to specific countries based on the end-user's location for products and the country in which the service is provided. Information with respect to the Company's geographic operations is set forth in the table below:

	Germany	United States	Rest of the World	Total
1998				
Net revenue external customers	305,210	2,562,603	637,863	3,505,676
Long-lived assets	33,832	478,801	258,779	771,412
1997				
Net revenue external customers	288,297	2,156,622	529,450	2,974,369
Long-lived assets	42,629	542,414	193,791	778,834
1996				
Net revenue external customers	354,719	759,877	304,939	1,419,535

$ in thousands

22. Supplementary Cash Flow Information

The following additional information is provided with respect to the Consolidated Financial Statement of Cash Flows:

	1998	1997	1996
Supplementary cash flow information			
Cash paid for interest	207,944	147,336	41,812
Cash paid for income taxes, net	(1,250)	88,955	7,098
Supplementary schedule of non-cash investing and financing activities			
Issuance of convertible investment securities for acquisitions	41,805	67,584	–
Issuance of preference shares for acquisitions	–	34,425	–
Contributions in kind from Fresenius AG	–	3,392	–
Acquisition of equipment through obligations under capital leases	521	10,529	7,375
Disposal of assets under capital leases	422	12,832	3,901
Details for acquisitions			
Assets acquired	286,413	572,973	4,085
Liabilities assumed	14,331	40,739	–
Notes issued in connection with acquisition	41,805	67,584	–
Preference shares issued in connection with acquisition	–	34,425	–
Contributions in kind from Fresenius AG	–	3,392	–
Cash paid	230,277	426,833	4,085
Less cash acquired	7,342	2,234	–
Net cash paid for acquisitions	**222,935**	**424,599**	**4,085**

$ in thousands

Report of the Supervisory Board

On a regular basis, the Managing Board apprised the Supervisory Board, both in writing and orally, of the progress of the Company's business and its financial performance and position as well as important business transactions. On the basis of the written and oral reports made by the Managing Board, the Supervisory Board adopted several resolutions in writing, by telephone and in four meetings. In particular, transactions requiring its approval were reviewed by the Supervisory Board and discussed with the Managing Board.

The main topics were the sale of the U.S. Homecare and Diagnostics businesses of Fresenius Medical Care North America, the stock option program for managerial staff and acquisitions. Furthermore, the Supervisory Board obtained detailed reports covering developments at the dialysis clinics acquired since the beginning of 1997. The Supervisory Board did not establish any committee during the reporting period.

The Supervisory Board examined the financial statements, the management report and the proposal for the appropriation of the net profits for the year, in each case for the 1998 fiscal year. These documents were reviewed in the presence of a representative from the Company's external auditor. Since the financial statements of the Company are part of the consolidated financial statements of Fresenius Aktiengesellschaft, Bad Homburg v.d.H., and the latter are deemed to be exempting consolidated financial statements pursuant to Section 291 HGB (German Commercial Code), the Company was not obligated to prepare (partially) consolidated financial statements in accordance with the German commercial law provisions. The accounting, the financial statements and the management report of Fresenius Medical Care AG for the 1998 fiscal year were audited by KPMG Deutsche Treuhandgesellschaft Aktiengesellschaft Wirschaftsprüfungsgesellschaft, Frankfurt am Main, – elected as auditors by a resolution of shareholders at the Annual General Meeting on June 10, 1998 and commissioned by the Supervisory Board – and bear the unqualified audit opinion. The auditors' reports were submitted to the Supervisory Board which acknowledged their receipt and approved their contents. No objections are to be raised to the financial statements of Fresenius Medical Care AG, even according to the final result of the review of the Supervisory Board itself.

In its meeting of April 14, 1999, the Supervisory Board approved the financial statements of Fresenius Medical Care AG for the 1998 financial year as submitted by the Managing Board, which thereby became final.

In accordance with Section 312 AktG (German Corporation Law), the Managing Board prepared a report for the 1998 fiscal year on its dealings with affiliated companies. The report contains the Managing Board's final statement that, in the transactions mentioned in the report, Fresenius Medical Care AG received adequate consideration under the circumstances known to the Managing Board at the time when such transactions were consummated and that no other measures within the meaning of Section 312 AktG were taken or omitted. The Supervisory Board reviewed this report and concurs with the auditor who added the following audit opinion to the report:

> "Following our proper review and judgement, we confirm that (1) the factual statements made in the report are correct, that (2) with respect to the transactions mentioned in the report, the consideration made by the company was not disproportionate or that any disadvantages have been offset and that (3) regarding the measures reported, no major objections are to be raised to the Managing Board's judgement."

Based on the final result of the review of the Supervisory Board, no objections are to be raised to the Managing Board's final statement as contained in the subordinate status report.

Mr. Donald Staheli resigned from his Supervisory Board seat at the end of 1998. The Supervisory Board thanks Mr. Staheli for his valuable contribution to this board.

The Supervisory Board thanks the Managing Board and all the employees for their efforts and achievements in 1998.

Bad Homburg v.d.H., April 14, 1999
The Supervisory Board

Dr. Gerd Krick
Chairman

Supervisory Board

Dr. Gerd Krick *Chairman*
Chief Executive Officer of Fresenius AG
Bad Homburg, Germany

Dr. Gerd Krick, 60, was appointed Chairman of the Supervisory Board effective January 1, 1998. Since 1992 he has been Chairman of the Fresenius AG Managing Board. Prior to 1992, he was Director of the Medical Systems Division of Fresenius AG and Vice Chairman of the Fresenius AG Managing Board. From September 1996 until December 1997, Dr. Krick was Chairman of the Managing Board of Fresenius Medical Care AG.

Dr. Dieter Schenk *Vice Chairman*
Attorney and tax advisor
Munich, Germany

Dr. Dieter Schenk, 46, is an attorney and tax advisor and has been a partner in the law firm of Nörr, Stiefenhofer & Lutz since 1986. Dr. Schenk is also a member and Vice Chairman of the Supervisory Board of Greiffenberger AG. Greiffenberger AG is a German corporation listed on the Munich Stock Exchange that manufactures specialty steel and machine tools.

Dr. Eckart O. Ebner
Public accountant and tax advisor
Stuttgart, Germany

Dr. Eckart O. Ebner, 60, is a public accountant and tax advisor and has been a partner in the accounting firm of Dr. Ebner, Dr. Stolz und Partner, Stuttgart, since 1974. Dr. Ebner is also a member of the Advisory Board of Drescher GmbH, Ruedesheim, an internationally operating communications company. He is also a member of the Advisory Committee of Georg Thieme Verlag, Stuttgart, an international publishing company.

Donald L. Staheli*
Former Chairman of the Board and Chief Executive Officer of Continental Grain Company
New York, USA
(until December 31, 1998)

Donald L. Staheli, 67, is the retired Chairman of the Board and Chief Executive Officer of Continental Grain Company, an international agribusiness and financial services concern. Mr. Staheli joined Continental Grain Company in 1969, and was elected President in 1984, Chief Executive Officer in 1988 and Chairman of the Board in 1994. Mr. Staheli serves as a Director of Prudential Life Insurance Company of America, Bankers Trust New York Corporation and ContiFinancial Corporation. He is Chairman of the U.S. China Business Council, a Director of the New York City Partnership, a member of the Council on Foreign Relations, and a member of the Board of Trustees for the American Graduate School of International Business.

Bernhard Walter
Member of the Managing Board of Dresdner Bank AG
Frankfurt/Main, Germany
(until June 10, 1998)

Bernhard Walter, 56, has been speaker of the Managing Board of Dresdner Bank AG since 1997 and a member of this board since 1987. Mr. Walter is also a member of the supervisory boards of various companies in Germany and other European countries. Mr. Walter retired from the Supervisory Board of the Company effective June 10, 1998.

Dr. Bernd Fahrholz
Lawyer, Member of the Managing Board of Dresdner Bank AG
Bad Homburg, Germany
(since June 10, 1998)

Dr. Bernd Fahrholz, 51, has been a member of the Managing Board of Dresdner Bank AG since 1998. Dr. Fahrholz is also a member of the supervisory boards of various companies.

Walter L. Weisman*
Former Chairman of the Board and Chief Executive Officer of American Medical International, Inc.
Beverly Hills, USA

Walter Weisman, 63, is a private investor and a former Chairman and Chief Executive Officer of American Medical International, Inc. (AMI). Mr. Weisman joined AMI in 1972, was elected President in 1979 and served as Chief Executive Officer from 1985 to 1988. Mr. Weisman is a Vice Chairman of the Board of the California Institute of Technology and Chairman of its Institute Relations Committee, a Trustee of Harvey Mudd College, a Trustee of the Los Angeles County Museum of Art, Chairman of the Board of the Sundance Institute, a Trustee of the Ashland Shakespeare Festival, and a Director of Price REIT, Inc. and Clinical Micro Sensors, Inc.

*Independent Director

Managing Board

Udo Werlé
Chairman
Lampertheim, Germany

Mr. Udo Werlé, 54, was appointed as Chairman of the Managing Board effective January 1, 1998. Mr. Werlé was Chief Financial Officer of the Company between October 1996 and end of 1997. Mr. Werlé has been Chief Financial Officer and Labor Relations Director of Fresenius AG since January 1994. Mr. Werlé was previously a member of the Managing Board of ABB Kraftwerke AG, Mannheim. In his last position as President of ABB Power Ventures Ltd., Zurich/Mannheim, he was responsible for all cooperation and joint ventures for the Power Generation segment. Mr. Werlé joined ABB Power Ventures Ltd. in 1970.

Ben J. Lipps, Ph. D.
Vice Chairman and Chief Executive Officer for North America
Boston, Massachusetts, USA

Dr. Ben J. Lipps, 58, has been Vice Chairman of Fresenius Medical Care AG's Managing Board since September 1998 and has been President, Chief Executive Officer and a Director of Fresenius Medical Care Holdings, Inc. since 1996. Prior to September 1996 Dr. Lipps served as President, Chief Executive Officer, Chief Operating Officer and a Director of Fresenius USA, Inc. ("FUSA") and in various executive capacities with FUSA's predecessor. Dr. Lipps joined Dow Chemical Company in 1966 and led the research team that developed the first hollow fiber dialyzer. Prior to joining FUSA's predecessor, Dr. Lipps was Vice President of Research and Development for Cordis Dow Corporation.

Roberto Fusté
Chief Executive Officer for Asia-Pacific (since January 1, 1999)
Hong Kong, China

Mr. Roberto Fusté, 46, was appointed to the Managing Board of Fresenius Medical Care AG effective January 1, 1999. Mr. Fusté is responsible for the Asia-Pacific area, for which he assumed responsibility in 1998. His business office is in Hong Kong. Mr. Fusté joined Fresenius in 1991 when Fresenius acquired Nephrocontrol S.A., a Spanish company which he founded in 1985 and of which he was Managing Director and joint owner. After the company was acquired by Fresenius, he continued as Managing Director. In 1995, he joined the Head Office of Fresenius where he has held various executive positions.

Dr. Emanuele Gatti
Chief Executive Officer for Europe, Middle East, Latin America and Africa
Bad Homburg, Germany

Dr. Emanuele Gatti, 43, has been a member of the Managing Board of Fresenius Medical Care AG since May 1997 and is President and Chief Executive Officer of Europe, Middle East, Latin America and Africa within the International segment. Previously he was Executive Vice President with responsibility for the dialysis business in Southern Europe. Dr. Gatti joined the Fresenius Group in 1989 when the Italian company Sis-Ter, of which he was the General Manager, was acquired by Fresenius AG. He has worked in the field of dialysis since 1981 after leaving the University of Milan where he was involved in teaching and biomedical research.

Hans-Ulrich Sutter
Chief Financial Officer
Bad Soden, Germany

Hans-Ulrich Sutter, 50, has been Chief Financial Officer of Fresenius Medical Care AG since July 1997. Mr. Sutter was previously a member of the management committee of the German subsidiary of the Procter & Gamble Company and had served that company for more than 24 years. In his last position, Mr. Sutter was responsible for the Finance and Controlling function of the European Tissue business of Procter & Gamble.

Products and Services of Fresenius Medical Care

A.N.D.Y. *PLUS*®
Disposable CAPD system: a non-disconnect-Y-system.

AQUA·PLUS·SYSTEM™
Water treatment and purification system to prepare water for dialysis.

AQUASAFE 08™
Reverse osmosis unit for the purification of raw water. Purified water is needed for the preparation of hemodialysis fluid.

AutoPRIME™
Option for the 4008 dialysis machine enabling online priming and rinsing of the extracorporeal circuit and online bolus infusion, i.e. infusion of a defined volume, with sterile fluid obtained by filtration of the dialysis fluid.

biBag®
Flexible bag containing dry bicarbonate powder to support online production of dialysis fluid with high microbiological quality.

Bicarbonate concentrate
Basic concentrate for bicarbonate hemodialysis.

BioAdequacy™
The concept of adequate patient care in the most biocompatible way aims to increase life expectancy and improve the quality of life and well-being of patients with kidney failure.

Biofine®
PVC-free material developed by Fresenius Medical Care. Foils, tubings and other components are produced with Biofine®.

Blood Temperature Monitor™ (BTM™)
Module for the hemodialysis machine to measure the blood temperature and to actively control the body temperature of dialysis patients.

Blood Volume Monitor™ (BVM™)
Module for the hemodialysis machine to measure the relative blood volume and to actively control fluid removal from the patient in order to reduce severe complications during dialysis treatment.

DIASAFE®
Filter for the purification of dialysis fluid during hemodialysis to obtain ultrapure dialysis fluid.

DIASAFE®*plus*
Optimized filter (see DIASAFE®) with a new design concept and increased retention capacity for water-borne microbial contaminants.

F10HPS
Low-flux hemodialyzer with an extra large surface area combining unsurpassed blood compatibility and outstanding clearances of small uremic toxins.

Freedom™ Cycler PD-PLUS
Automated cycling machine used to provide peritoneal dialysis therapy.

Fresenius Polysulfone® dialyzer
Dialyzer containing the unique Fresenius Polysulfone® membrane.

Granudial®
Dry granulated bicarbonate, acid and acetate concentrates for the in-house production of liquid concentrates.

H*d*F100S
Large surface area hemodiafilter especially suited for convective therapies with high exchange volumes.

IQcard™
The IQcard is used with the Freedom Cycler PD-PLUS to monitor every minute of automated peritoneal dialysis therapy. Provides integrated data for patient evaluation and research models.

Lia® (Laboratory Information Access)
The most advanced ESRD laboratory data management system in the dialysis industry, applying computer technology to the delivery and analysis of laboratory results.

On-line Clearance (OLC) / On-line Clearance Monitor (OCM)
Optional component of a hemodialysis machine to measure online the effective in vivo dialyzer clearance for quality assurance purposes.

ONLINE *plus*™ system
A newly introduced system for Fresenius Medical Care's 4008 series hemodialysis machines to perform online hemodiafiltration and online hemofiltration. Infusion fluid is prepared from dialysate by filtration in a convenient and cost-effective way.

PD-PLUS™ therapy
Special form of Automated Peritoneal Dialysis (APD) where cycler-supported nocturnal dialysate exchanges are combined with a dialysate exchange during the daytime.

***sleep•safe*™**
The new automated peritoneal dialysis system from Fresenius Medical Care offering the full range of peritoneal dialysis options and a maximum of safety and comfort for the patient, physician and nurse.

***stay•safe*®**
Completely PVC-free peritoneal dialysis system which is biocompatible, safe and environmentally-friendly.

Healthcare and Dialysis Related Terms

Anemia
Reduced oxygen transport capacity of the blood, measured as reduced content of hemoglobin in the blood.

Automated Peritoneal Dialysis (APD)
Machine (cycler)-supported version of peritoneal dialysis treatment usually performed during the night.

Biocompatibility
Quality of a material, device, system or solution to avoid any adverse reaction in the patient.

Blood lines
System of tubes connecting the patient's blood circulation with the dialyzer during dialysis treatment.

CE certification
Mark which demonstrates compliance with the directives of the European Union for medical devices.

Clearance
A quantitative parameter to describe dialyzer performance in terms of uremic toxin removal.

Continuous ambulatory peritoneal dialysis (CAPD)
A treatment method of peritoneal dialysis. The peritoneal dialysis solution is exchanged manually, generally four times per day.

Convective therapies
Therapies such as hemofiltration (HF) or hemodiafiltration (HDF) using high ultrafiltration fluxes to improve the removal of high molecular weight solutes.

Cycler
Machine managing automated peritoneal dialysis treatment.

Dialysate
Fluid used in the process of dialysis. The concentration of each component is set depending on the desired direction and amount of its transport.

Dialysis
Form of renal replacement therapy, where a semi-permeable membrane is used for solute transport, i.e. in peritoneal dialysis the peritoneum of the patient and in hemodialysis the membrane of the dialyzer.

Dialyzer
Special filter used in hemodialysis for removing toxic substances and excess water from the blood. It is sometimes referred to as the 'artificial kidney'.

End-stage renal disease (ESRD)
Disease of patients with terminal kidney failure accompanied by long-term complications such as renal anemia, hypertension and other cardiovascular problems, bone disease, loss of appetite and malnutrition.

Erythropoietin (EPO)
Protein that stimulates red blood cell production. Recombinant human EPO is commonly prescribed to patients on dialysis who suffer from anemia.

Health Maintenance Organization (HMO)
Special form of private health insurance in the U.S. where the insured persons are members, and the treatments are provided by contracted physicians (or member physicians) of the organization.

Hemodiafiltration (HDF)
Special mode of ESRD treatment, combining advantages of hemodialysis and hemofiltration, i.e. high elimination rates for small and large molecular weight substances.

Hemodialysis (HD)
Treatment mode for ESRD, where the blood of the patient is purified using a dialyzer. The solute exchange between blood and dialysate is dominated by diffusive processes.

Hemofiltration (HF)
ESRD treatment mode, where no dialysate is used. The solutes are removed following convective forces by filtering plasma water through a semipermeable membrane. The volume removed by filtering is balanced by substitution fluid.

High-flux dialyzers
Dialyzers containing highly permeable membranes allowing the effective removal of water and large uremic toxins such as β_2-microglobulin.

Kidney failure, acute
Acute loss of renal function. There is a good chance for the recovery of renal function, if the cause of acute kidney failure can be eliminated. Depending on the severity of renal function loss, intermittent dialysis treatment may be necessary.

Kidney failure, chronic
Chronic loss of renal function, also referred to as end-stage renal disease. The recovery of renal function is not possible, thus the patient has to be treated with renal replacement therapy, i.e. kidney transplantation or dialysis.

Managed Care Organization
See Health Maintenance Organization.

Management Services Organization (MSO)
An administrative organization that acquires physician groups and provides them with an infrastructure that typically includes practice management and claims management, in exchange for a fee.

Peritoneal dialysis
Dialysis treatment method using the patient's peritoneum as a 'filter' for the purification of the blood.

Peritoneal dialysis system
System comprising bags and lines for introduction and drainage of a solution to and from the abdominal cavity of the patient.

Peritoneal dialysis solution
Solution introduced into the abdominal cavity of the patient to absorb toxins and excess water.

Peritoneum
A smooth, soft skin which covers the inner surface of the abdominal cavity and the abdominal organs.

Ultrafiltration rate
Rate of fluid removal from the patient's blood circulation. This rate has to be chosen carefully. If the rate is too high, the cardiovascular stability of the patient is put at risk; if it is too low, the necessary amount of excess water cannot be removed from the patient.

Uremic toxins
A variety of chemical substances which increasingly accumulate in the blood of a patient when kidney function becomes insufficient. Uremic toxins are considered to be the major cause of the clinical symptoms related to uremia.

Vascular access
Mode of connecting the patient's blood circulation to the dialyzer. The vascular access must allow sufficient blood flows and connection as often as necessary, normally three times weekly.

Financial Terms

American Depositary Receipt (ADR)
Share certificate traded at the New York Stock Exchange, representing (parts of) shares of a foreign company.

DAX
The DAX index comprises 30 German blue chip stocks, quoted on the Frankfurt stock exchange. The criteria for including the stock of a corporation in the DAX are the volume of trading in its stock and its market capitalization.

EBIT
Earnings before interest and taxes – corresponding to operating income.

EBITDA
Earnings before interest, taxes, depreciation and ammortisation – corresponding to cash flow before taxes.

Euro (€)
With the beginning of stage three of the European Monetary Union, conversion factors between the currencies of the eleven member states were set irrevocably on January 1, 1999. One euro equals 1.95583 Deutsche Mark. Starting on January 4, the German stock exchange has quoted share prices in euros.

Market capitalization
Number of shares multiplied by the share price.

MDAX
Stock index combining 70 medium-sized publicly-traded German companies which follow the 30 largest German companies ranked by market capitalization and trading volume.

Ordinary and preference shares
The capital stock of the Company is divided into ordinary and preference shares. Both are bearer shares. Preference shares are non-voting, but are entitled to a dividend that exceeds that for the ordinary shares, and the distribution of the minimum dividend on the preference shares has precedence over the distribution of a dividend on the ordinary shares.

STOXX
Pan-European stock index created in 1998. It includes the 650 biggest European companies.

U.S. GAAP
United States Generally Accepted Accounting Principles.

Working capital
Current assets minus current liabilities.

The financial statements of Fresenius Medical Care AG will be included in the consolidated financial statements of Fresenius AG. Fresenius Medical Care AG is therefore not required to prepare consolidated financial statements under German GAAP. Fresenius Medical Care filed an annual report under Form 20-F with the Securities and Exchange Commission (SEC) with additional information on the Company. Fresenius Medical Care's annual report on Form 20-F may be obtained from the Company or by shareholders in the United States by writing to:

ADR Service Center
P.O. Box 8205
Boston, MA 02266-8205

Tel. (800) 428-4237

The audited financial statement of the Group's holding company, Fresenius Medical Care Aktiengesellschaft, will be published in the German Federal Gazette (Bundesanzeiger) and can be obtained from the Company.