MCKESSON CORP
Form DEF 14A
June 15, 2012
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of the Securities

Exchange Act of 1934 (Amendment No.)

Filed by the Registrant þ

Filed by a Party other than the Registrant ¨

Check the appropriate box:

¨ Preliminary Proxy Statement

¨ **Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**

þ Definitive Proxy Statement

¨ Definitive Additional Materials

¨ Soliciting Material Pursuant to §240.14a-12

McKesson Corporation

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

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þ No fee required.

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NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

OF McKESSON CORPORATION

The 2012 Annual Meeting of Stockholders of McKesson Corporation will be held on Wednesday, July 25, 2012 at 8:30 a.m. at the Crown Plaza Hotel, 1221 Chess Drive, Foster City, California to:

Elect for a one-year term a slate of nine directors as nominated by the Board of Directors;

Ratify the appointment of Deloitte & Touche LLP as the Company s independent registered public accounting firm for the fiscal year ending March 31, 2013;

Conduct a non-binding, advisory vote on executive compensation;

Vote on four proposals submitted by stockholders, if properly presented; and

Conduct such other business as may properly be brought before the meeting.

Stockholders of record at the close of business on May 31, 2012 are entitled to notice of and to vote at the meeting or any adjournment or postponement of the meeting.

By Order of the Board of Directors

Willie C. Bogan

Associate General Counsel and Secretary

One Post Street

San Francisco, California 94104-5296

June 15, 2012

YOUR VOTE IS IMPORTANT.

We encourage you to read the proxy statement and vote your shares as soon as possible. You may vote via the Internet or by telephone. Specific instructions on how to vote using either of these methods are included on the proxy card. You may also vote by mail, and a return envelope for your proxy card is enclosed for your convenience.

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PROXY STATEMENT

General Information

Proxies and Voting at the Annual Meeting

The Board of Directors of McKesson Corporation (the Company, McKesson, we or us), a Delaware corporation, is soliciting proxies to be voted at the Annual Meeting of Stockholders to be held July 25, 2012 (the Annual Meeting), and at any adjournment or postponement thereof. This proxy statement includes information about the matters to be voted upon at the Annual Meeting.

On June 15, 2012, the Company began delivering proxy materials to all stockholders of record at the close of business on May 31, 2012 (the Record Date). On the Record Date, there were 236,187,328 shares of the Company s common stock outstanding and entitled to vote. As a stockholder, you are entitled to one vote for each share of common stock you held on the Record Date, including shares: (i) held for you in an account with a broker, bank or other nominee; (ii) held directly in your name as the stockholder of record; or (iii) allocated to your account in the Company s Profit-Sharing Investment Plan (the PSIP).

If you have shares held by a broker, bank or other nominee, you can vote your shares by following the instructions provided by your broker, bank or other nominee. If you are a stockholder of record or a participant in the Company s PSIP, you can vote your shares by using the Internet, by calling a toll-free number, or by mailing your signed proxy card(s). Specific instructions for voting by means of the Internet or telephone are located on the enclosed proxy card. The Internet and telephone voting procedures are designed to authenticate each stockholder s identity and to allow each stockholder to vote his or her shares and confirm that his or her voting instructions have been properly recorded. If you do not wish to vote via the Internet or by telephone, please complete, sign and return the proxy card in the self-addressed, postage-paid envelope provided.

You can revoke your proxy at any time before the Annual Meeting by sending to the Company s Secretary a written revocation or a proxy bearing a later date. You may also revoke your proxy by attending the Annual Meeting in person and casting a ballot. If you hold your shares through a broker, bank or other nominee and have instructed the broker, bank or other nominee as to how to vote your shares, you must obtain a legal proxy and bring it to the meeting in order to change your vote or to vote at the Annual Meeting. Please contact your broker, bank or other nominee for specific information on how to obtain a legal proxy in order to vote your shares at the meeting.

Your vote as a stockholder is important. Please vote as soon as possible to ensure that your vote is recorded.

All shares represented by valid proxies will be voted as specified. If you sign and return a proxy card without specific voting instructions, your shares will be voted as recommended by our Board of Directors (the Board or the Board of Directors) on all proposals described in this proxy statement, and in the discretion of the designated proxy holders as to any other matters that may properly come before the Annual Meeting. We currently know of no other matter to be presented at the Annual Meeting, except for the proposals described in this proxy statement.

All votes cast at the Annual Meeting will be tabulated by Broadridge Financial Solutions, Inc. (Broadridge), which has been appointed the independent inspector of election. Broadridge will determine whether or not a quorum is present.

Attendance at the Annual Meeting

You will need to bring your admission ticket and any valid government-issued form of identification if you plan to attend the Annual Meeting. You will find an admission ticket attached to the proxy card if you are a registered stockholder or PSIP participant. If your shares are held in the name of a broker, bank or other stockholder of record and you plan to attend the Annual Meeting in person, you may obtain an admission ticket in advance by sending a request, along with proof of ownership, such as a brokerage or bank account statement, to the Company s Secretary, One Post Street, 35th Floor, San Francisco, California 94104. Stockholders who do not have an admission ticket will only be admitted upon verification of ownership.

Dividend Reinvestment Plan

For those stockholders who participate in the Company s Automatic Dividend Reinvestment Plan (DRP), the enclosed proxy card includes all full shares of common stock held in your DRP account on the Record Date for the Annual Meeting, as well as your shares held of record.

Vote Required and Method of Counting Votes

Each share of the Company s common stock you own entitles you to one vote at the Annual Meeting. You may vote for or against one or more of the director nominees, or abstain from voting on the election of any nominee. A nominee will be elected as a director if he or she receives a majority of votes cast (that is, the number of votes cast for a director nominee must

exceed the number of votes cast against that nominee). Abstentions or broker non-votes (as described below), if any, will not count as votes cast. There is no cumulative voting with respect to the election of directors.

For all other items to be presented at the Annual Meeting, approval of each of these proposals requires the affirmative vote of a majority of the shares present, in person or by proxy, and entitled to vote on the proposal at the Annual Meeting. You may vote for or against, or abstain from voting on, each of these other proposals. Shares represented by abstentions on a proposal will be counted as present at the Annual Meeting and will have the effect of a vote against the matter; however, broker non-votes with respect to a proposal will have no effect on the outcome of the matter.

The Board recommends a vote FOR each nominee named in Item 1, and FOR Items 2 and 3, and AGAINST Items 4 through 7.

Voting Results of the Annual Meeting

We intend to announce preliminary voting results at the Annual Meeting, and publish preliminary results or, if available, final results in a Current Report on Form 8-K to be filed with the Securities and Exchange Commission (the SEC) within four business days after the Annual Meeting.

Quorum Requirement

The presence in person or by proxy of holders of a majority of the outstanding shares of common stock entitled to vote will constitute a quorum for the transaction of business at the Annual Meeting. In the event of abstentions or broker non-votes, the shares represented will be considered present for quorum purposes.

Broker Non-Votes

Generally, broker non-votes occur when a broker, bank or other nominee does not have discretion to vote on a proposal without specific instructions from the beneficial owner and instructions are not given. New York Stock Exchange (NYSE) rules prohibit discretionary voting by brokers on certain matters. At the Annual Meeting, if brokers, banks and other nominees have not received instructions from the beneficial owners, they will not be permitted to vote on any proposal other than the ratification of the appointment of the independent registered public accounting firm (Item 2).

Therefore, we encourage all beneficial owners to provide voting instructions to your nominees to ensure that your shares are voted at the Annual Meeting.

Profit-Sharing Investment Plan

Participants in the Company s tax qualified 401(k) plan, the PSIP, have the right to instruct the PSIP trustee, on a confidential basis, how the shares allocated to their accounts are to be voted, and will receive a voting instruction card for that purpose. In general, the PSIP provides that all shares for which no voting instructions are received from participants and unallocated shares of common stock held in the employee stock ownership plan established as part of the PSIP, will be voted by the trustee in the same proportion as shares for which voting instructions are received. However, shares that have been allocated to PSIP participants PAYSOP accounts for which no voting instructions are received will not be voted.

List of Stockholders

The names of stockholders of record entitled to vote at the Annual Meeting will be available at the meeting and for ten days prior to the meeting for any purpose germane to the Annual Meeting, during ordinary business hours, at our principal executive offices at One Post Street, 35th Floor, San Francisco, California. You may obtain this information by contacting the Secretary of the Company.

Online Access to Annual Reports on Form 10-K and Proxy Statements

The notice of annual meeting, proxy statement and Annual Report on Form 10-K for our fiscal year ended March 31, 2012 are available at *www.proxyvote.com*. Instead of receiving future copies of the proxy statement and Annual Report on Form 10-K by mail, you may, by following the applicable procedures described below, elect to receive these documents electronically, in which case you will receive an e-mail with a link to these documents.

Stockholders of Record: You may elect to receive proxy materials electronically next year in place of printed materials by logging on to *www.proxyvote.com* and entering your control number, which you can locate on the accompanying proxy card. By doing so, you will save the Company printing and mailing expenses, reduce the impact on the environment and obtain immediate access to the Annual Report on Form 10-K, proxy statement and voting form when they become available.

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Beneficial Stockholders: If you hold your shares through a broker, bank or other holder of record, you may also have the opportunity to receive copies of the proxy statement and Annual Report on Form 10-K electronically. Please check the information provided in the proxy materials mailed to you by your broker, bank or other holder of record regarding the availability of this service or contact the broker, bank or other holder of record through which you hold your shares and inquire about the availability of such an option for you.

If you elect to receive your materials via the Internet, you can still request paper copies by leaving a message with Investor Relations at (800) 826-9360 or by sending an e-mail to *investors@mckesson.com.*

Householding of Proxy Materials

In a further effort to reduce printing costs, postage fees and the impact on the environment, we have adopted a practice approved by the SEC called householding. Under this practice, stockholders who have the same address and last name and do not participate in electronic delivery of proxy materials will receive only one copy of our proxy materials, unless any of these stockholders notifies us that he or she wishes to continue receiving individual copies. Stockholders who participate in householding will continue to receive separate proxy cards.

If you share an address with another stockholder and received only one set of proxy materials, but would like to request a separate copy of these materials, please contact Broadridge by calling (800) 542-1061 or by writing to Broadridge, Householding Department, 51 Mercedes Way, Edgewood, New York 11717. Similarly, you may also contact Broadridge if you received multiple copies of the proxy materials and would prefer to receive a single copy in the future.

PROPOSALS TO BE VOTED ON

Item 1. ***Election of Directors***

There are nine nominees for election to the Board of Directors of the Company. The directors elected at the Annual Meeting will hold office until the 2013 Annual Meeting of Stockholders and until their successors have been elected and qualified, or until their earlier death, resignation or removal.

All nominees are existing directors and were elected to the Board at the 2011 Annual Meeting of Stockholders. For purposes of the upcoming Annual Meeting, the Committee on Directors and Corporate Governance (sometimes referred to as the Governance Committee) recommended the reelection of each nominee as a director. Each nominee has informed the Board that he or she is willing to serve as a director. If any nominee should decline or become unable or unavailable to serve as a director for any reason, your proxy authorizes the persons named in the proxy to vote for a replacement nominee, if the Board names one, as such persons determine in their best judgment. As an alternative, the Board may reduce the number of directors to be elected at the Annual Meeting.

Majority Voting Standard for Election of Directors. The Company s Amended and Restated By-laws (the By-laws) provide for a majority voting standard for the election of directors in uncontested director elections, such as that being conducted this year. Under this standard, a director nominee will be elected only if the number of votes cast for the nominee exceeds the number of votes cast against that nominee. In the case of contested elections (a situation in which the number of nominees exceeds the number of directors to be elected), the plurality vote standard will apply. This majority voting standard is described further below under the section entitled Corporate Governance Majority Voting Standard.

The following is a brief description of the age, principal occupation, position and business experience, including other public company directorships, for at least the past five years and major affiliations of each of the nominees. Each director s biographical information includes a description of the director s experience, qualifications, attributes or skills that qualify the director to serve on the Company s Board at this time.

Nominees

Your Board recommends a vote FOR each Nominee.

ANDY D. BRYANT, Chairman of the Board, Intel Corporation

Mr. Bryant, age 62, was elected Chairman of the Board of Intel Corporation in May 2012. He was named a director of Intel s board in July 2011 and served as Vice Chairman of the Board from that time until his election as Chairman. He served as Executive Vice President and Chief Administrative Officer of Intel from October 2007 to July 2011. Mr. Bryant joined Intel in 1981 and held a number of management positions before serving as Intel s Chief Financial Officer from February 1994 to October 2007. He is also a director of Columbia Sportswear Company and Kryptiq Corporation. He was formerly a director of Synopsys Inc. Mr. Bryant has been a director of the Company since January 2008. He is Chair of the Finance Committee and a member of the Audit Committee.

Mr. Bryant s years of experience as an executive at a large global company, including as Chief Administrative Officer and Chief Financial Officer, provide to the Company s Board operational, strategic planning and financial expertise and considerable business acumen, as well as international business experience. We believe the Company benefits from his Board leadership perspective garnered from serving as both Vice Chair and Chairman of Intel s Board. Mr. Bryant also has other public company board experience with service on audit and governance committees. In addition, having joined the Company s Board in 2008, Mr. Bryant has brought a valuable fresh perspective to the Board.

WAYNE A. BUDD, Senior Counsel, Goodwin Procter LLP

Mr. Budd, age 70, joined the law firm of Goodwin Procter LLP as Senior Counsel in October 2004. He had been Senior Executive Vice President and General Counsel and a director of John Hancock Financial Services, Inc. since 2000 and a director of John Hancock Life Insurance Company since 1998. From 1996 to 2000, Mr. Budd was Group President-New England for Bell Atlantic Corporation (now Verizon Communications, Inc.). From 1994 to 1997, Mr. Budd was a Commissioner, United States Sentencing Commission and from 1993 to 1996, he was a senior partner at the law firm of Goodwin Procter LLP. From 1992 to 1993, he was the Associate Attorney General of the United States and from 1989 to 1992, he was United States Attorney for the District of Massachusetts. Mr. Budd has been a director of the Company since October 2003. He is a member of the Audit Committee and the Committee on Directors and Corporate Governance.

Mr. Budd brings to our Board significant legal and regulatory expertise gained from years of large law firm practice and major governmental positions with law enforcement responsibilities. His legal experience and seasoned judgment have been instrumental in helping the Board navigate legal challenges. In recognition of his distinguished legal career and important contributions to public life, Mr. Budd was named a 2011 recipient of the American Lawyer Lifetime Achievement Award. Additionally, Mr. Budd has senior executive business experience and public company board experience with service on audit, governance, compensation, and special litigation committees.

JOHN H. HAMMERGREN, Chairman of the Board, President and Chief Executive Officer

Mr. Hammergren, age 53, has served as Chairman of the Board since July 2002, and President and Chief Executive Officer of the Company since April 2001. Mr. Hammergren joined the Company in 1996 and held a number of management positions before becoming President and Chief Executive Officer. He is also a director of the Hewlett-Packard Company. He has been a director of the Company since July 1999.

Including his experience at other significant healthcare organizations prior to joining the Company, Mr. Hammergren brings to the Board over 30 years of business and leadership experience in healthcare, as well as public company board experience. In addition to the strong leadership skills exhibited as Chief Executive Officer of the Company, he recently served as Chairman of the Healthcare Leadership Council, a coalition of chief executives of the nation s leading healthcare companies and organizations. His healthcare industry and general business perspective have been broadened through his membership on this council, on the Business Council and on the Business Roundtable. The Board benefits from Mr. Hammergren s extensive knowledge of the Company, and from his deep understanding of its customer base, workforce, competition, challenges and opportunities.

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ALTON F. IRBY III, Chairman and Founding Partner, London Bay Capital

Mr. Irby, age 71, was the founding partner and has been Chairman of London Bay Capital, a privately-held investment firm, since May 2006. He was the founding partner of Tricorn Partners LLP, a privately-held investment bank from May 2003 to May 2006, a partner of Gleacher & Co. Ltd. from January 2001 until April 2003, and Chairman and Chief Executive Officer of HawkPoint Partners, formerly known as National Westminster Global Corporate Advisory, from 1997 until 2000. He was a founding partner of Hambro Magan Irby Holdings from 1988 to 1997. He serves as a director of Stifel Financial Corporation and an indirect wholly-owned subsidiary of the Company, McKesson Information Solutions UK Limited. He was formerly a director of Catlin Group PLC, Centaur Holdings PLC and ContentFilm PLC. Mr. Irby has been a director of the Company since January 1999. He is Chair of the Compensation Committee and a member of the Finance Committee.

Mr. Irby has 40 years of experience as a senior executive of financial services companies, and 35 years of service on various private and public company boards. During this time, he has acquired significant international business experience and demonstrated entrepreneurial talent as the founding partner of several firms. Based on his overall experience, Mr. Irby is able to provide to the Company s Board valuable insights into financial and capital market matters, acquisition opportunities and divestiture considerations.

M. CHRISTINE JACOBS, Chairman of the Board, President and Chief Executive Officer, Theragenics Corporation

Ms. Jacobs, age 61, is the Chairman, President and Chief Executive Officer of Theragenics Corporation, a manufacturer of prostate cancer treatment devices and surgical products. She has held the position of Chairman since May 2007, and previously from 1998 to 2005. She was Co-Chairman of the Board from 1997 to 1998 and was elected President in 1992 and Chief Executive Officer in 1993. Ms. Jacobs has been a director of the Company since January 1999. She is a member of the Compensation Committee and the Committee on Directors and Corporate Governance.

Having led a public company within the healthcare industry for 20 years, Ms. Jacobs brings to our Board significant relevant industry experience and a keen understanding of and strong insight into issues, challenges and opportunities facing the Company, including those related to legislative healthcare initiatives. As a Chairman and Chief Executive Officer, she is at the forefront of her company in regard to the evolving corporate governance environment, which enables her to provide valuable contributions as a member of the Governance Committee of our Board. Since September 2011, Ms. Jacobs has served as Co-Chair of the newly formed Securities and Exchange Commission Advisory Committee on Small and Emerging Companies, which reflects recognition of her leadership experience. She will serve a term of three years on the Advisory Committee.

MARIE L. KNOWLES, Executive Vice President and Chief Financial Officer, Retired, ARCO

Ms. Knowles, age 65, retired from Atlantic Richfield Company (ARCO) in 2000 and was Executive Vice President and Chief Financial Officer from 1996 until 2000 and a director from 1996 until 1998. She joined ARCO in 1972. Ms. Knowles is also a member of the Board of Trustees of the Fidelity Funds. She has been a director of the Company since March 2002. She is Chair of the Audit Committee and a member of the Finance Committee.

Ms. Knowles brings to the Board extensive financial experience gained through her career at ARCO, including her tenure as Chief Financial Officer. This experience makes her well qualified to serve as Chair of the Company s Audit Committee and as the audit committee financial expert. This experience also enables Ms. Knowles to provide critical insight into, among other things, the Company s financial statements, accounting principles and practices, internal control over financial reporting, and risk management processes.

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David M. Lawrence, M.D., Chairman of the Board and Chief Executive Officer, Retired, Kaiser Foundation Health Plan, Inc. and Kaiser Foundation Hospitals

Dr. Lawrence, age 71, retired as Chief Executive Officer and Chairman of Kaiser Foundation Health Plan, Inc. and Kaiser Foundation Hospitals in December 2002. He served as Chairman of the Board from 1992 to May 2002 and Chief Executive Officer from 1991 to May 2002 of Kaiser Foundation Health Plan, Inc. and Kaiser Foundation Hospitals. He held a number of management positions with these organizations prior to assuming these positions, including Vice Chairman of the Board and Chief Operating Officer. He is also a director of Agilent Technologies Inc. He was formerly a director of Raffles Medical Group, Inc., PG&E Corporation and Dynavax Technologies Corporation. Dr. Lawrence has been a director of the Company since January 2004. He is a member of the Compensation Committee and the Finance Committee.

Dr. Lawrence possesses considerable leadership experience in the healthcare industry, having served for a decade as Chairman and Chief Executive Officer of one of the largest private healthcare systems in the world. This experience, coupled with his training as a physician, enables him to provide an important perspective and valuable insight into various aspects of the Company s businesses. In addition, Dr. Lawrence brings to our Board broad experience and perspective gained through his considerable public company board experience, including his service on compensation, audit, finance and governance committees.

Edward A. Mueller, Chairman of the Board and Chief Executive Officer, Retired, Qwest Communications International Inc.

Mr. Mueller, age 65, retired as Chairman and Chief Executive Officer of Qwest Communications International Inc., a provider of voice, data and video services, in April 2011. He held the position of Chairman and Chief Executive Officer of Qwest Communications from August 2007 to April 2011. From January 2003 until July 2006, he served as Chief Executive Officer of Williams-Sonoma, Inc., a provider of specialty products for cooking. Prior to joining Williams-Sonoma, Inc., Mr. Mueller served as President and Chief Executive Officer of Ameritech Corporation, a subsidiary of SBC Communications, Inc., from 2000 to 2002. He is also a director of The Clorox Company. He was formerly a director of CenturyLink, Inc., Williams-Sonoma, Inc. and VeriSign, Inc. Mr. Mueller has been a director of the Company since April 2008. He is a member of the Compensation Committee and the Committee on Directors and Corporate Governance.

Mr. Mueller brings to the Board chief executive leadership and business management experience, as well as a strong business acumen and strategic planning expertise. Having worked outside the healthcare industry, he also adds to the mix of experiences and perspectives on our Board that promote a robust deliberative and decision-making process. While Chairman of the Board of Qwest Communications, Mr. Mueller had a leadership role in corporate governance, which enables him to provide valuable contributions as a member of the Governance Committee of our Board. He also has public company board experience with audit committee service. In addition, having joined the Company s Board in 2008, Mr. Mueller has brought a valuable fresh perspective to the Board.

Jane E. Shaw, Ph.D., Chairman of the Board, Retired, Intel Corporation; Chairman of the Board and Chief Executive Officer, Retired, Aerogen, Inc.

Dr. Shaw, age 73, retired as the non-executive Chairman of the Board of Intel Corporation in May 2012. She had held that position since May 2009. Dr. Shaw retired as Chairman of the Board of Aerogen, Inc., a company specializing in the development of products for improving respiratory therapy, in October 2005. She had held that position since 1998. She retired as Chief Executive Officer of that company in June 2005. She is also a director of AeroSurgical Limited. She was formerly a director of Talima Therapeutics, Inc. and OfficeMax Incorporated. Dr. Shaw has been a director of the Company since April 1992. She is Chair of the Committee on Directors and Corporate Governance and a member of the Audit Committee.

As a former Chief Executive Officer, Dr. Shaw brings to the Board executive leadership and business management experience in the healthcare industry. She also has a strong financial background, which positions her well to serve on the Audit Committee. Dr. Shaw gained valuable board leadership experience as former executive Chairman of Aerogen, Inc. and former non-executive Chairman of Intel Corporation. This experience also makes her well qualified to serve as Chair of the Governance Committee, and she has played a major role in helping the Company navigate the changing governance landscape.

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Having been raised and educated in Europe, she also has an international background that broadens the Board s perspective. As the longest-standing Board member, the Board benefits from her considerable institutional knowledge. It is also noteworthy that Dr. Shaw was named a 2010 Outstanding Director by the Outstanding Directors Exchange.

The Board, Committees and Meetings

The Board of Directors is the Company s governing body with responsibility for oversight, counseling and direction of the Company s management to serve the long-term interests of the Company and its stockholders. The Board s goal is to build long-term value for the Company s stockholders and to ensure the vitality of the Company for its customers, employees and other individuals and organizations that depend on the Company. To achieve its goals, the Board monitors both the performance of the Company and the performance of the Chief Executive Officer (CEO). The Board currently consists of nine members, all of whom are independent with the exception of the Chairman.

The Board has, and for many years has had, standing committees: currently, the Audit Committee, the Compensation Committee, the Committee on Directors and Corporate Governance, and the Finance Committee. Each of these committees is governed by a written charter approved by the Board in compliance with the applicable requirements of the SEC and the NYSE listing requirements (collectively, the Applicable Rules). The charter of each committee requires an annual review by such committee. Each member of our standing committees is independent, as determined by the Board, under the NYSE listing standards and the Company s director independence standards. In addition, each member of the Audit Committee meets the additional, heightened independence criteria applicable to audit committee members, as established by the SEC. The members of each standing committee are appointed by the Board each year for a term of one year or until their successors are elected. The membership of each standing committee and the number of meetings held during the fiscal year ended March 31, 2012 (FY 2012) is identified in the table below.

Director	Audit	Compensation	Directors and Corporate Governance	Finance
Andy D. Bryant	X			Chair
Wayne A. Budd	X		X	
John H. Hammergren				
Alton F. Irby III		Chair		X
M. Christine Jacobs		X	X	
Marie L. Knowles	Chair			X
David M. Lawrence, M.D.		X		X
Edward A. Mueller		X	X	
Jane E. Shaw, Ph.D.	X		Chair	
Number of meetings held during FY 2012	**6**	**6**	**3**	**4**

In addition, the Board has, on occasion, established committees to deal with particular matters the Board believes appropriate to be addressed in that manner.

Board and Meeting Attendance

The Board met eight times during FY 2012. Each director attended at least 75% of the aggregate number of meetings of the Board and of all the standing and other committees on which he or she served. Directors meet their responsibilities not only by attending Board and committee meetings, but also through communication with executive management, independent accountants, advisors and consultants and others on matters affecting the Company. Directors are also expected to attend the upcoming Annual Meeting, and all directors attended the Annual Meeting of Stockholders held in July 2011.

Audit Committee

The Audit Committee is responsible for, among other things, reviewing with management the annual audited financial statements filed in the Annual Report on Form 10-K, including any major issues regarding accounting principles and practices as well as the adequacy and effectiveness of internal control over financial reporting that could significantly affect the Company s financial statements; reviewing with management and the independent registered public accounting firm (the independent accountants) the interim financial statements prior to the filing of the Company s quarterly reports on Form 10-Q; the appointment of the independent accountants; monitoring the independence and

evaluating the performance of the independent accountants; approving the fees to be paid to the independent accountants; reviewing and accepting the annual audit plan, including the scope of the audit activities of the independent accountants; at least annually reassessing the adequacy of the Audit Committee s charter and recommending to the Board any proposed changes; reviewing major changes to the Company s accounting principles and practices; reviewing the appointment, performance, and replacement of the senior internal audit department executive; advising

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the Board with respect to the Company s policies and procedures regarding compliance with applicable laws and regulations and with the Company s code of conduct; and performing such other activities and considering such other matters, within the scope of its responsibilities, as the Audit Committee or Board deems necessary or appropriate. The composition of the Audit Committee, the attributes of its members, including the requirement that each be financially literate and have other requisite experience, and the responsibilities of the Audit Committee, as reflected in its charter, are in accordance with the Applicable Rules for corporate audit committees.

Audit Committee Financial Expert

The Board has designated Ms. Knowles as the Audit Committee s financial expert and has determined that she meets the qualifications of an audit committee financial expert in accordance with SEC rules, and that she is independent as defined for audit committee members in the listing standards of the NYSE and applicable SEC requirements, and in accordance with the Company s director independence standards.

Compensation Committee

The Compensation Committee has responsibility for, among other things, reviewing all matters relating to CEO compensation, including making and annually reviewing decisions concerning cash and equity compensation, and other terms and conditions of employment for the CEO, incorporating the review of the CEO s performance against pre-established business and individual objectives that is conducted annually by the full Board; reviewing and approving corporate goals and objectives relating to compensation of other executive officers, and making and annually reviewing decisions concerning the cash and equity compensation, and other terms and conditions of employment for those executive officers; reviewing and making recommendations to the Board with respect to adoption of, or amendments to, all equity-based incentive compensation plans and arrangements for employees and cash-based incentive plans for executive officers, including an evaluation of whether the relationship between the incentives associated with these plans and the level of risk-taking by executive officers in response to such incentives is reasonably likely to have a material adverse effect on the Company; subject to any authority the Compensation Committee, the Board or the applicable stock plan document may have delegated to others, approving grants of stock, stock options, stock purchase rights or other equity grants to employees eligible for such grants; interpreting the Company s stock plans; reviewing its charter annually and recommending to the Board any changes the Compensation Committee determines are appropriate; participating with management in the preparation of the Compensation Discussion and Analysis for the Company s proxy statement; and performing such other activities required by applicable law, rules or regulations, and consistent with its charter, as the Compensation Committee or the Board deems necessary or appropriate. The Compensation Committee may delegate to any officer or officers the authority to grant awards to employees other than directors or executive officers, provided that such grants are within the limits established by the Delaware General Corporation Law and by resolution of the Board. The Compensation Committee determines the structure and amount of all executive officer compensation, including awards of equity, after considering the initial recommendation of management and in consultation with the Compensation Committee s independent compensation consultant.

The Compensation Committee directly employs its own independent compensation consultant, Compensation Strategies, Inc., and independent legal counsel, Gunderson Dettmer Stough Villeneuve Franklin & Hachigian, LLP. These advisors do not provide any other services to the Company, except that Compensation Strategies, Inc. also provides consulting services to the Governance Committee in the area of director compensation. In accordance with its charter, the Compensation Committee annually evaluates the qualifications, performance and independence of its advisors. Additional information on the Compensation Committee s process and procedures for consideration of executive compensation is addressed in the Compensation Discussion and Analysis below.

Finance Committee

The Finance Committee has responsibility for, among other things, reviewing the Company s dividend policy; reviewing the adequacy of the Company s insurance programs; reviewing with management the long-range financial policies of the Company; providing advice and counsel to management on the financial aspects of significant acquisitions and divestitures, major capital commitments, proposed financings and other significant transactions; making recommendations concerning significant changes in the capital structure of the Company; reviewing tax planning strategies utilized by management; reviewing the funding status and investment policies of the Company s tax-qualified retirement plans; and reviewing and (when authorized by the Board) approving the principal terms and conditions of securities that may be issued by the Company.

Committee on Directors and Corporate Governance

The Governance Committee has responsibility for, among other things, recommending guidelines and criteria to be used to select candidates for Board membership; reviewing the size and composition of the Board to assure that proper skills and experience are represented; recommending the slate of nominees to be proposed for election at the annual meeting of stockholders;

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recommending qualified candidates to fill Board vacancies; evaluating the Board s overall performance; developing and administering the Company s related party transactions policy; advising the Board on matters of corporate governance, including the Corporate Governance Guidelines and composition of committees; and advising the Board regarding director compensation and administering the 2005 Stock Plan with respect to directors equity awards.

Director Qualifications, Nomination and Diversity

To fulfill its responsibility to recruit and recommend to the full Board nominees for election as directors, the Governance Committee considers all qualified candidates who may be identified by any one of the following sources: current or former Board members, a professional search firm, Company executives or stockholders. Stockholders who wish to propose a director candidate for consideration by the Governance Committee may do so by submitting the candidate s name, resume and biographical information and qualifications to the attention of the Secretary of the Company at One Post Street, 35th Floor, San Francisco, California 94104. All proposals for recommendation or nomination received by the Secretary will be presented to the Governance Committee for its consideration. The Governance Committee and the Company s CEO will interview those candidates who meet the criteria described below, and the Governance Committee will recommend to the Board nominees that best suit the Board s needs. In order for a recommended director candidate to be considered by the Governance Committee for nomination for election at an upcoming annual meeting of stockholders, the recommendation must be received by the Secretary not less than 120 days prior to the anniversary date of the Company s most recent annual meeting of stockholders.

In evaluating candidates for the Board, the Governance Committee reviews each candidate s biographical information and credentials, and assesses each candidate s independence, skills, experience and expertise based on a variety of factors. Members of the Board should have the highest professional and personal ethics, integrity and values consistent with the Company s values. They should have broad experience at the policy-making level in business, technology, healthcare or public interest, or have achieved national prominence in a relevant field as a faculty member or senior government officer. The Governance Committee will consider whether the candidate has had a successful career that demonstrates the ability to make the kind of important and sensitive judgments that the Board is called upon to make, and whether the candidate s skills are complementary to the existing Board members skills. Board members must take into account and balance the legitimate interests and concerns of all of the Company s stockholders and other stakeholders, and each must be able to devote sufficient time and energy to the performance of his or her duties as a director, as well as have a commitment to diversity.

The Governance Committee has responsibility under its charter to review annually with the Board the size and composition of the Board with the objective of achieving the appropriate balance of knowledge, experience, skills, expertise and diversity required for the Board as a whole. Although the Board does not maintain a formal policy regarding diversity, the Governance Committee considers diversity to include diversity of backgrounds, cultures, education, experience, skills, thought, perspectives, personal qualities and attributes, and geographic profiles (*i.e.*, where the individuals have lived and worked), as well as race, ethnicity, gender, national origin and other categories. A high level of diversity on our Board has been achieved in these areas, as evidenced by the information concerning our directors that is provided under Nominees above. Our Governance Committee and Board believe that a diverse representation on the Board fosters a robust, comprehensive, and balanced deliberative and decision-making process that is essential to the continued effective functioning of the Board and continued success of the Company.

Director Compensation

The Company believes that compensation for non-employee directors should be competitive and should encourage ownership of the Company s stock. The compensation for each non-employee director of the Company includes an annual cash retainer, an annual restricted stock unit (RSU) award and per-meeting fees. With regard to committees other than standing committees, the Board determines on a case-by-case basis whether meeting fees are appropriate for non-employee directors. The Board currently has established a $1,500 per-meeting fee in each case in which it determines a meeting fee is appropriate. In addition to the compensation described above, the Presiding Director and chairs of the standing committees receive an annual retainer. Non-employee directors are paid their reasonable expenses for attending Board and committee meetings. Directors who are employees of the Company or its subsidiaries do not receive any compensation for service on the Board. The Governance Committee annually reviews the level and form of the Company s director compensation and, if it deems appropriate, recommends to the Board changes in director compensation.

Cash Compensation

Director annual retainers and meeting fees are paid in cash. Directors may elect in advance of a calendar year to defer up to 100% of their annual retainer (including any standing committee chair or Presiding Director retainer) and meeting fees into the Company s Deferred Compensation Administration Plan III (DCAP III). The minimum deferral period for any amounts deferred is five years; however, notwithstanding the director s deferral election, if a director ceases to be a director of the Company for any reason other than death, disability or retirement, the account balance will be paid in a lump sum in the first

January or July which is at least six months following and in the year after his or her separation from service. In the event of death, disability or retirement, the account balance will be paid in accordance with the director s deferral election. To be eligible for retirement, a director must have served on the Board for at least six consecutive years prior to his or her separation. The Compensation Committee approves the interest rates to be credited each year to amounts deferred into the DCAP III, which currently are (i) 8.0% per annum for amounts deferred prior to January 1, 2010, and (ii) 120% of the long-term applicable federal rate as published each year in December by the U.S. Internal Revenue Service, for amounts deferred on or after January 1, 2010.

The following table summarizes the cash compensation provided to non-employee directors:

Non-Employee Director Cash Compensation	
Annual cash retainer	$ 75,000
Additional retainer for Presiding Director	$ 10,000
Additional retainer for Chair of the Audit Committee	$ 20,000
Additional retainer for Chair of the Compensation Committee	$ 20,000
Additional retainer for Chair of all other standing committees	$ 10,000
Meeting fee for each Audit Committee meeting attended	$ 2,000
Meeting fee for each Board or other committee meeting attended	$ 1,500

Equity Compensation

Each July, non-employee directors receive an automatic annual grant of RSUs with an approximate value as of the grant date equal to $150,000. The actual number of RSUs granted is determined by dividing $150,000 by the closing price of the Company s common stock on the grant date (with any fractional unit rounded up to the nearest whole unit); provided, however, that the number of units granted in any annual grant will in no event exceed 5,000, in accordance with our 2005 Stock Plan.

The RSUs granted to non-employee directors are vested upon grant. If a director meets the director stock ownership guidelines (currently $300,000 in shares and share equivalents), then the director will, on the grant date, receive the shares underlying the RSUs, unless the director elects to defer receipt of the shares. The determination of whether a director meets the director stock ownership guidelines is made as of the last day of the deferral election period preceding the applicable RSU award. If a non-employee director has not met the stock ownership guidelines as of the last day of such deferral election period, then payment of the shares underlying the RSUs will automatically be deferred until the director s separation from service.

Recipients of RSUs are entitled to dividend equivalents at the same dividend rate applicable to the Company s common stockholders, which currently is $0.20 per share each quarter. For our directors, dividend equivalents on the RSUs are credited quarterly to an interest-bearing cash account and are not distributed until the shares underlying the RSUs are issued to the director. Interest accrues on directors credited dividend equivalents at the rate set by the Compensation Committee under the terms of our 2005 Stock Plan, which for calendar year 2012 is 8.0% per annum.

All Other Compensation and Benefits

Non-employee directors are eligible to participate in the McKesson Foundation s Executive Request Program and Matching Gifts Program. Under these programs, our non-employee directors may request that the foundation make donations to qualifying public charitable organizations, and our non-employee directors own gifts to schools, educational associations or funds, and other public charitable organizations are eligible for a match by the foundation up to $5,000 per director for each fiscal year.

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2012 Director Compensation Table

The following table sets forth information concerning the compensation paid to or earned by each non-employee director for the fiscal year ended March 31, 2012. Mr. Hammergren, our Chairman of the Board, President and Chief Executive Officer, is not included in this table as he is an employee of the Company and thus receives no compensation for his service as a director. The compensation paid to or earned by Mr. Hammergren as an officer of the Company is shown in the 2012 Summary Compensation Table.

Name	Fees Earned or Paid in Cash ($)[1]	Stock Awards ($)[2]	Change in Pension Value and Nonqualified Deferred Compensation Earnings ($)[3]	All Other Compensation ($)[4]	Total ($)
Andy D. Bryant	110,000	150,065	9,144		269,209
Wayne A. Budd	120,000	150,065	24,806	5,000	299,871
Alton F. Irby III	123,500	150,065	26,183		299,748
M. Christine Jacobs	100,500	150,065	3,341		253,906
Marie L. Knowles	140,500	150,065	15,846		306,411
David M. Lawrence, M.D.	104,000	150,065	8,122	5,000	267,187
Edward A. Mueller	100,500	150,065	7,869		258,434
Jane E. Shaw, Ph.D.	120,500	150,065	16,304		286,869

(1) Consists of the following, as applicable, whether paid or deferred (including for Mr. Irby $1,500 for his service as a board member of McKesson Information Solutions UK Limited): director annual retainer; standing committee meeting fees; other committee meeting fees; and the annual standing committee chair and Presiding Director retainers.

(2) Represents the aggregate grant date fair value of RSUs, including the value of any dividend equivalents, computed in accordance with Accounting Standards Codification issued by the Financial Accounting Standards Board, Topic 718, labeled Compensation Stock Compensation (ASC Topic 718) disregarding any estimates of forfeitures related to service-based vesting conditions. Such values do not reflect whether the recipient has actually realized a financial benefit from the award. For information on the assumptions used to calculate the value of the awards, refer to Financial Note 3 of the Company s consolidated financial statements in its Annual Report on Form 10-K for the fiscal year ended March 31, 2012, as filed with the SEC on May 2, 2012. For awards that are not subject to performance conditions, such as those provided to directors, the maximum award level would not result in an award greater than what is disclosed in the table above.

(3) Represents the amount of above-market interest earned under the Company s Deferred Compensation Administration Plans and above-market interest credited on undistributed dividend equivalents. As defined by the SEC, above-market interest is any amount over 120% of the long-term applicable federal rate as published by the U.S. Internal Revenue Service. A discussion of the Company s Deferred Compensation Administration Plans is provided below in the subsection entitled Narrative Disclosure to the 2012 Nonqualified Deferred Compensation Table.

(4) For Messrs. Budd and Lawrence, represents the amount of donations and matching charitable contributions provided by the McKesson Foundation.

Corporate Governance

The Board is committed to, and for many years has adhered to, sound and effective corporate governance practices. The Board is also committed to diligently exercising its oversight responsibilities with respect to the Company s business and affairs consistent with the highest principles of business ethics, and to meeting the corporate governance requirements of both federal law and the NYSE. In addition to its routine monitoring of best practices, each year the Board and its committees review the Company s current corporate governance practices, the corporate governance environment and current trends, and update their written charters and guidelines as necessary. The Board has adopted independence standards

for its members, Corporate Governance Guidelines, as well as charters for the Audit, Compensation, Finance and Governance Committees, all of which can be found on the Company s website at *www.mckesson.com* under the caption Investors Corporate Governance and are described more fully below.

Majority Voting Standard for Election of Directors

The By-Laws provide for a majority voting standard for the election of directors. This standard states that in uncontested director elections, a director nominee will be elected only if the number of votes cast for the nominee exceeds the number of votes cast against that nominee. To address the holdover director situation in which, under Delaware law, a director remains on the Board until his or her successor is elected and qualified, the By-Laws require each director nominee to submit an irrevocable resignation in advance of the stockholder vote. The resignation would be contingent upon both the nominee not receiving the required vote for reelection and acceptance of the resignation by the Board pursuant to its policies.

If a director nominee receives more against votes for his or her election, the Board s Governance Committee, composed entirely of independent directors, will evaluate and make a recommendation to the Board with respect to the tendered resignation. In its review, the Governance Committee will consider, by way of example, the following factors: the impact of the acceptance of the resignation on stock exchange listing or other regulatory requirements; the financial impact of the acceptance of the resignation; the unique qualifications of the director whose resignation has been tendered; the reasons the Governance Committee believes that stockholders cast votes against the election of such director (such as a vote no campaign on an illegitimate or wrongful basis); and any alternatives for addressing the against votes.

The Board must take action on the Governance Committee s recommendation within 90 days following certification of the stockholders vote. Absent a determination by the Board that it is in the best interests of the Company for an unsuccessful incumbent to remain on the Board, the Board shall accept the resignation. The majority vote standard states that the Board expects an unsuccessful incumbent to exercise voluntary recusal from deliberations of the Governance Committee or the Board with respect to the tendered resignation. In addition, the standard requires the Company to file a current report on Form 8-K with the SEC within four business days after the Board s acceptance or rejection of the resignation, which must include an explanation of the reasons for any rejection of the tendered resignation. Finally, the standard also provides procedures to address the situation in which a majority of the members of the Governance Committee are unsuccessful incumbents or all directors are unsuccessful incumbents.

If the Board accepts the resignation of an unsuccessful incumbent director, or if in an uncontested election a nominee for director who is not an incumbent director does not receive a majority vote, the Board may fill the resulting vacancy or decrease the size of the Board. In contested elections, the plurality vote standard will apply. A contested election is an election in which a stockholder has duly nominated a person to the Board and has not withdrawn that nomination at least five days prior to the first mailing of the notice of the meeting of stockholders.

Elimination of Supermajority Voting Requirements

In furtherance of the Governance Committee s commitment to periodically evaluate the Company s governing documents to determine if any changes are advisable, in 2011, the Board recommended, and the stockholders approved, amendments to the Company s Amended and Restated Certificate of Incorporation (the Certificate of Incorporation) and, in effect, the Company s By-Laws to eliminate the Company s stockholder supermajority voting requirements. Specifically, the Company replaced the supermajority voting requirement with a majority of shares outstanding standard for the following actions: (i) amendment of the By-Laws and (ii) amendment of the Certificate of Incorporation in any manner that would adversely affect holders of Series A Junior Participating Preferred Stock. In addition, the supermajority voting provisions and associated fair price provisions applicable to certain business combinations were eliminated from the Certificate of Incorporation altogether.

Codes of Business Conduct and Ethics

The Company is committed to the highest standards of ethical and professional conduct and has adopted a Code of Business Conduct and Ethics that applies to all directors, officers and employees, and provides guidance for conducting the Company s business in a legal, ethical and responsible manner. In addition, the Company has adopted a Code of Ethics applicable to the Chief Executive Officer, Chief Financial Officer, Controller and Financial Managers (Senior Financial Managers Code) that supplements the Code of Business Conduct and Ethics on certain topics. Both of the Codes are available on the Company s website at *www.mckesson.com* under the caption Investors Corporate Governance. The Company intends to post any amendment to, or waiver from, its Senior Financial Managers Code on its website within four business days after any such amendment or waiver.

Related Party Transactions Policy

The Company has a written Related Party Transactions Policy requiring approval or ratification of certain transactions involving executive officers, directors and nominees for director, beneficial owners of more than five percent of the Company s common stock, and immediate family members of any such persons where the amount involved exceeds $100,000. Under the policy, the Company s General Counsel initially determines if a transaction or relationship constitutes a transaction that requires compliance with the policy or disclosure. If so, the matter will be referred to the CEO for consideration with the General Counsel as to approval or ratification in the case of other executive officers and/or their immediate family members, or to the Governance Committee in the case of transactions involving directors, nominees for director, the General Counsel, the CEO or holders of more than five percent of the Company s common stock and/or their immediate family members. Annually directors, nominees and executive officers are asked to identify any transactions that might fall under the policy as well as identify immediate family members. Additionally, they are required to notify the General Counsel promptly of any proposed related party transaction. The policy is administered by the Governance Committee. The transaction may be ratified or approved if it is fair and reasonable to the Company and consistent with its best interests. Factors that may be taken into account in making that determination include:

(i) the business purpose of the transaction; (ii) whether it is entered into on an arms-length basis; (iii) whether it would impair the independence of a director; and (iv) whether it would violate the provisions of the Company s Code of Business Conduct and Ethics.

The Company and its subsidiaries may, in the ordinary course of business, have transactions involving more than $100,000 with unaffiliated companies of which certain of the Company s directors are directors and/or executive officers. Therefore, under the policy, the Governance Committee reviews such transactions. However, the Company does not consider the amounts involved in such transactions to be material in relation to its businesses, the businesses of such other companies or the interests of the directors involved. In addition, the Company believes that such transactions are on the same terms generally offered by such other companies to other entities in comparable transactions.

Corporate Governance Guidelines

The Board has long adhered to directorship practices designed to ensure effective corporate governance. Consistent with NYSE listing requirements, the Board has adopted the McKesson Corporation Corporate Governance Guidelines, which address various governance matters, including, among others: director qualification standards and the director nomination process; stockholder communications with directors; director responsibilities; selection and role of the Presiding Director; director access to management and, as necessary and appropriate, independent advisors; director compensation; director stock ownership guidelines; director orientation and continuing education; management succession; and an annual performance evaluation of the Board. The Governance Committee is responsible for overseeing the guidelines and annually assesses the need for any amendments to the guidelines to reflect corporate governance best practices, as necessary or appropriate. Our Corporate Governance Guidelines can be found on the Company s website at *www.mckesson.com* under the caption Investors Corporate Governance.

Director Stock Ownership Guidelines

Our Board believes that directors should hold a meaningful equity stake in McKesson. To that end, by the terms of our Director Stock Ownership Guidelines, directors are expected to own shares or share equivalents of the Company s common stock with a value not less than four times the annual board retainer within three years of joining our Board. We believe these terms serve the important purpose of aligning our directors economic interests with those of the stockholders. As of May 31, 2012, all of our directors were in compliance with the Director Stock Ownership Guidelines.

Director Independence

Under the Company s Corporate Governance Guidelines, the Board must have a substantial majority of directors who meet the applicable criteria for independence required by the NYSE. The Board must determine, based on all relevant facts and circumstances, whether in its business judgment, each director satisfies the criteria for independence, including the absence of a material relationship with the Company, either directly or indirectly. Consistent with the continued listing requirements of the NYSE, the Board has established standards to assist it in making a determination of director independence. A director will not be considered independent if:

- The director is, or has been within the last three years, an employee of the Company, or an immediate family member is, or has been within the last three years, an executive officer, of the Company.

- The director has received, or has an immediate family member who has received, during any twelve-month period within the last three years, more than $120,000 in direct compensation from the Company, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service).

- (A) The director is a current partner or employee of a firm that is the Company s internal or external auditor; (B) the director has an immediate family member who is a current partner of such a firm; (C) the director has an immediate family member who is a current employee of such a firm and personally works on the Company s audit; or (D) the director or an immediate family member was within the last three years a partner or employee of such a firm and personally worked on the Company s audit within that time.

The director or an immediate family member is, or has been within the last three years, employed as an executive officer of another company where any of the Company s present executive officers at the same time serves or served on that company s compensation committee.

The director is an executive officer or an employee, or whose immediate family member is an executive officer, of another company (A) which in any of the last three years accounted for at least 2.0% of the Company s consolidated gross revenues, or (B) for which in any such year the Company accounted for at least 2.0% or $1,000,000, whichever is greater, of such other company s consolidated gross revenues.

The director is, or has been within the last three years, an executive officer of another company that is indebted to the Company, or to which the Company is indebted, and the total amount of either company s indebtedness to the other is more than 2.0% of the respective company s total assets measured as of the last completed fiscal year.

The director serves, or served within the last three years, as an executive officer, director or trustee of a charitable organization, and the Company s discretionary charitable contributions in any single fiscal year exceeded the greater of $1,000,000 or 2.0% of that organization s total annual charitable receipts. (The Company s matching of employee charitable contributions will not be included in the amount of the Company s contributions for this purpose.)

For relationships not covered by the guidelines above, or for relationships that are covered, but as to which the Board believes a director may nonetheless be independent, the determination of independence shall be made by the directors who satisfy the NYSE independence rules and the guidelines set forth above. However, any determination of independence for a director who does not meet these standards must be specifically explained in the Company s proxy statement.

These standards can also be found on the Company s website at *www.mckesson.com* under the caption Investors Corporate Governance. Provided that no relationship or transaction exists that would disqualify a director under these standards, and no other relationship or transaction exists of a type not specifically mentioned in these standards that, in the Board s opinion, taking into account all relevant facts and circumstances, would impair a director s ability to exercise his or her independent judgment, the Board will deem such person to be independent. Applying these standards, and all applicable laws, rules or regulations, the Board has determined that, with the exception of John H. Hammergren, all of the current directors, namely Andy D. Bryant, Wayne A. Budd, Alton F. Irby III, M. Christine Jacobs, Marie L. Knowles, David M. Lawrence, Edward A. Mueller and Jane E. Shaw, are independent.

Succession Planning

In accordance with our Corporate Governance Guidelines, the Board is responsible for approving and maintaining a succession plan for the CEO and other executive officers. To assist the Board with this requirement, the Company s Executive Vice President, Human Resources annually leads the Board of Directors in a discussion of CEO and senior management succession. This meeting is held in an executive session of the full Board, with the Executive Vice President, Human Resources present. The annual review includes an evaluation of the requirements for the CEO and each senior management position, and an examination of potential permanent and interim candidates for CEO and senior management positions. In order to minimize disruption in operations of the Company in the event of a temporary or permanent absence of the CEO, including in emergency situations, the Board adopted a CEO Absence Event Management Process. This process establishes clear procedures for planning for and responding to a CEO absence event, while maintaining the Board s ability to exercise its judgment and discretion in such event, including with regard to the selection of an interim or permanent replacement CEO.

Executive Sessions of the Board

The independent directors of the Board meet in executive session without members of management present on a regularly scheduled basis. The members of the Board designate a Presiding Director to preside at such executive sessions. The Presiding Director position rotates annually each July among all independent directors. The Presiding Director establishes the agenda for each executive session and also determines which, if any, other individuals, including members of management and independent advisors, should attend each such meeting. The Presiding Director also, in collaboration with the Chairman and the Secretary, reviews the agenda in advance of the Board of Directors meetings. Dr. Lawrence is the current Presiding Director until his successor is chosen by the other independent directors at the Board s meeting in July 2012.

Board Leadership Structure

Mr. Hammergren serves as our Chairman of the Board and Chief Executive Officer. The Company does not have a policy regarding whether the Chairman and CEO roles should be combined or separated. Rather, the Company s Corporate Governance Guidelines retain flexibility for the Board to choose its Chairman in any way that it deems best for the Company at any given time. The Board periodically reviews the appropriateness and effectiveness of its leadership structure given numerous factors. Although the Company has in the past separated the roles of Chairman and CEO, the Board believes that having Mr. Hammergren serve as both Chairman and CEO, coupled with strong independent director leadership, is the most appropriate and effective Board leadership structure for the Company at this time.

A number of factors support the current leadership structure. Mr. Hammergren has over 30 years of experience in the healthcare industry, and has served as the Chairman and CEO of the Company for ten years. The Board believes that Mr. Hammergren s in-depth knowledge of the healthcare industry and of the complex businesses and operations of the Company best equips him to lead Board meetings as the directors

discuss key business and strategic matters and best equips him to focus the Board on the most critical issues. The current combined Chairman and CEO structure has promoted decisive leadership, ensured clear accountability and enhanced our ability to communicate with a single and consistent voice to stockholders, customers, employees

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and other stakeholders. During the time Mr. Hammergren has served as both Chairman and CEO, the Company has achieved outstanding financial results as displayed in the Compensation Discussion and Analysis below.

In addition, the Board believes that other aspects of the current leadership structure and Corporate Governance Guidelines ensure effective independent Board leadership and oversight of management. For example, the Board regularly meets in executive session without the CEO or any other members of management present, and an independent director serves as the Presiding Director at such sessions. Additionally, in accordance with the Company s Corporate Governance Guidelines, the Chairman consults with the Presiding Director regarding agenda topics, and consistent with the Guidelines, other directors are invited to, and in fact do, suggest items for inclusion on the Board and committee meeting agendas. As a matter of practice, the Chairman regularly elicits input from all of the independent directors as to the matters they would like covered at the meetings and the information they would find most helpful in their deliberations and decision-making. Strong independent director leadership is also enhanced by the fact that all of the Board s standing committees are composed solely of, and chaired by, independent directors.

The Board s role in risk oversight is discussed in greater detail below; however, with respect to the Board s leadership structure, the Board believes that the current structure is consistent with, and indeed enhances the effectiveness of, its risk oversight role. In short, Mr. Hammergren s extensive management experience and in-depth knowledge of the healthcare industry and of the complex businesses and operations of the Company, as discussed above, also assist the Board in understanding the risks facing the Company and, therefore, in more effectively performing its risk oversight function.

In sum, the Company s existing Board leadership structure strikes an effective balance between strong, strategically advantageous Chairman and CEO leadership, and appropriate oversight of management provided by strong independent directors. The combined Chairman and CEO structure has served the Company and its stockholders well, and remains the most appropriate leadership structure for the Company at this time.

Board of Directors Role in Risk Oversight

The Company s management is responsible for the day-to-day management of the risks facing the Company, including macroeconomic, financial, strategic, operational, public reporting, legal, regulatory, political, compliance, and reputational risks. Management carries out this risk management responsibility through a coordinated effort among the various risk management functions within the Company.

Under our By-Laws and Corporate Governance Guidelines, the Board has responsibility for overseeing the business and affairs of the Company. This general oversight responsibility includes oversight of risk management, which the Board carries out as a whole or through its committees. Among other things, the Board as a whole periodically reviews the Company s enterprise risk management processes for identifying, ranking and assessing risks across the organization, as well as the output of that process. The Board as a whole also receives periodic reports from the Company s management on various risks, including risks facing the Company s businesses. Although the Board has ultimate responsibility for overseeing risk management, it has delegated to its committees certain oversight responsibilities. For example, in accordance with its charter, the Audit Committee engages in ongoing discussions regarding major financial risk exposures and the process and system employed to monitor and control such exposures. In addition, consistent with its charter, the Audit Committee engages in periodic discussions with management concerning the process by which risk assessment and management are undertaken. In carrying out these responsibilities, the Audit Committee, among other things, regularly reviews with the head of Internal Audit the audits or assessments of significant risks conducted by Internal Audit personnel based on their audit plan; and the committee regularly meets in executive sessions with the head of Internal Audit. The Audit Committee also regularly reviews with the Controller the Company s internal control over financial reporting, including any significant deficiencies. As part of the reviews involving Internal Audit and the Controller, the Audit Committee reviews steps taken by management to monitor, control and mitigate risks. The Audit Committee also regularly reviews with the General Counsel and Chief Compliance Officer significant legal, regulatory, and compliance matters that could have a material impact on the Company s financial statements or business. Finally, from time to time executives who are responsible for managing a particular risk report to the Audit Committee on how the risk is being controlled and mitigated.

The Board has also delegated to other committees the responsibility to oversee risk within their areas of responsibility and expertise. For example, the Finance Committee exercises oversight with regard to the risk assessment and management processes related to, among other things, credit, capital structure, liquidity, insurance programs and the Company s retirement and 401(k) plans. As noted in the section below entitled Risk Assessment of Compensation Policies and Practices, the Compensation Committee oversees risk assessment and management with respect to the Company s compensation policies and practices.

In those cases in which committees have risk oversight responsibilities, the Chairs of the committees regularly report to the full Board the significant risks facing the Company, as identified by management, and the measures undertaken by management for controlling and mitigating those risks.

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Risk Assessment of Compensation Policies and Practices

We annually conduct a review of all incentive compensation plans utilized throughout the Company, using a framework for risk assessment provided to us by a nationally-recognized outside compensation advisor. In conducting our review, a detailed assessment of each incentive compensation plan, without regard to materiality, is first prepared by representatives from the Company s business units and then reviewed by senior executives of our Human Resources Department. The review framework requires representatives of our business units to examine and report on the presence of certain design elements under both cash and equity incentive compensation plans that could encourage our employees to incur excessive risk, such as the selection and documentation of incentive metrics, the ratio of incentive to fixed compensation, the year-over-year variability in payouts, the amount of management discretion, and the percentage of compensation expense as compared to the business units revenues. Consistent with our findings in past years, management concluded that for FY 2012 our policies and practices do not create risks that are reasonably likely to have a material adverse effect on the Company. A summary of management s findings was reviewed with the Compensation Committee at its May 2012 meeting.

The Compensation Committee discussed management s findings, and considered that the Company s compensation programs contain many design features that mitigate the likelihood of encouraging excessive risk-taking behavior. These features include:

- A balance of fixed and variable compensation, with variable compensation tied to both short-term objectives and the long-term value of our stock price;
- Multiple metrics in our incentive programs across the entire enterprise that balance top-line, bottom-line and cash management objectives;
- Linear payout curves and caps in our incentive program payout formulas;
- Reasonable goals and objectives in our incentive programs;
- Modification of payouts based upon individual performance, inclusive of assessments against our ICARE principles (*i.e.*, integrity, customer first, accountability, respect and excellence);
- The Compensation Committee s ability to exercise downward discretion in determining incentive program payouts;
- Strong compensation recoupment provisions (*i.e.*, clawbacks) pertaining to all forms of incentive compensation;
- Stock ownership and retention guidelines applicable to our senior leadership team; and
- Training on our Code of Business Conduct and Ethics and other policies that educate our employees on appropriate behaviors and the consequences of taking inappropriate actions.

Based on the foregoing, the Compensation Committee concurred with management that our compensation policies and practices do not create inappropriate or unintended significant risk to the Company as a whole. We believe that our incentive compensation arrangements do not provide incentives that encourage risk-taking beyond the organization s ability to effectively identify and manage significant risks, are compatible with effective internal controls and the risk management practices of the Company, and are supported by the oversight and administration of the Compensation Committee with regard to executive compensation programs.

Communications with Directors

Stockholders and other interested parties may communicate with the Presiding Director, the non-management directors, or any of the directors by addressing their correspondence to the Board member or members, c/o the Corporate Secretary s Department, McKesson Corporation, One Post Street, 35th Floor, San Francisco, California 94104, or via e-mail to *presidingdirector@mckesson.com* or to *nonmanagementdirectors@mckesson.com.* The Board has instructed the Secretary, prior to forwarding any correspondence, to review such correspondence and, in his discretion, not to forward certain items if they are irrelevant to or inconsistent with the Company s operations, policies and philosophies, are deemed of a commercial or frivolous nature, or are otherwise deemed inappropriate for the Board s consideration. The Corporate Secretary s Department maintains a log of correspondence received by the Company that is addressed to members of the Board, other than advertisements, solicitations or correspondence deemed by the Secretary to be junk mail, of a frivolous nature, or otherwise not appropriate to retain. Members of the Board may review the log at any time, and request copies of any correspondence received.

Indemnity Agreements

The Company has entered into separate indemnity agreements with its directors and executive officers that provide for defense and indemnification against any judgment or costs assessed against them in the course of their service. Such agreements do not, however, permit indemnification for acts or omissions for which indemnification is not permitted under Delaware law.

Item 2. ***Ratification of Appointment of Deloitte & Touche LLP as the Company s Independent Registered Public Accounting Firm for Fiscal Year 2013***

Your Board recommends a vote FOR this ratification proposal.

The Audit Committee of the Company s Board of Directors has approved Deloitte & Touche LLP (D&T) as the Company s independent registered public accounting firm to audit the consolidated financial statements of the Company and its subsidiaries for the fiscal year ending March 31, 2013. D&T is knowledgeable about the Company s operations and accounting practices, and is well qualified to act as the Company s independent registered public accounting firm.

We are asking our stockholders to ratify the selection of D&T as the Company s independent registered public accounting firm. Although ratification is not required by our By-Laws or otherwise, the Board is submitting the selection of D&T to our stockholders for ratification as a matter of good corporate practice. If stockholders fail to ratify the selection, the Audit Committee will reconsider whether or not to retain D&T. Even if the selection is ratified, the Audit Committee in its discretion may select a different registered public accounting firm at any time during the year if it determines that such a change would be in the best interests of the Company and our stockholders. Representatives of D&T are expected to be present at the Annual Meeting to respond to appropriate questions and to make a statement if they desire to do so. For the fiscal years ended March 31, 2012 and 2011, professional services were performed by D&T, the member firms of Deloitte Touche Tohmatsu, and their respective affiliates (collectively, Deloitte & Touche), which includes Deloitte Consulting. Fees paid for those years were as follows:

	2012	2011
Audit Fees	$ 7,428,916	$ 6,836,542
Audit-Related Fees	1,601,519	3,070,907
Total Audit and Audit-Related Fees	**9,030,435**	**9,907,449**
Tax Fees	1,631,783	547,465
All Other Fees		
Total	**$ 10,662,218**	**$ 10,454,914**

Audit Fees. This category consists of fees billed for professional services rendered for the audit of the Company s consolidated annual financial statements, the audit of the Company s internal control over financial reporting as required by the Sarbanes-Oxley Act of 2002, review of the interim consolidated financial statements included in quarterly reports, and services that are normally provided by D&T in connection with statutory and regulatory filings or engagements. This category also includes advice on accounting matters that arose during, or as a result of, the audit or the review of interim financial statements, foreign statutory audits required by non-U.S. jurisdictions, registration statements and comfort letters.

Audit-Related Fees. This category consists of fees billed for professional services rendered in connection with the performance of an audit or reviews of the Company s consolidated financial statements and is not reported under Audit Fees. This includes fees for employee benefit plan audits, accounting consultations, due diligence in connection with mergers and acquisitions, attest services related to financial reporting that are not required by statute or regulation, and consultations concerning financial accounting and reporting standards.

Tax Fees. This category consists of fees billed for professional services rendered for U.S. and international tax compliance, including services related to the preparation of tax returns. For the fiscal years ended March 31, 2012 and 2011, no amounts were incurred by the Company for tax advice, planning or consulting services.

All Other Fees. This category consists of fees for products and services other than the services reported above. The Company paid no fees in this category for the fiscal years ended March 31, 2012 and 2011.

Policy on Audit Committee Pre-Approval of Audit and Permissible Non-Audit Services of Independent Registered Public Accounting Firm

Pursuant to the Applicable Rules, and as set forth in the terms of its charter, the Audit Committee has sole responsibility for appointing, setting compensation for, and overseeing the work of the independent registered public accounting firm. The Audit Committee has established a policy that requires it to pre-approve all audit and permissible non-audit services, including audit-related and tax services to be provided by Deloitte & Touche. Between meetings, the Chair of the Audit Committee is authorized to pre-approve services, which are reported to the committee at its

next meeting. All of the services described in the fee table above were approved in conformity with the Audit Committee s pre-approval process.

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Audit Committee Report

The Audit Committee of the Company s Board of Directors assists the Board in fulfilling its responsibility for oversight of the quality and integrity of the Company s financial reporting processes. The functions of the Audit Committee are described in greater detail in the Audit Committee s written charter adopted by the Company s Board of Directors, which may be found on the Company s website at *www.mckesson.com* under the caption Investors Corporate Governance. The Audit Committee is composed exclusively of directors who are independent under the applicable SEC and NYSE rules and the Company s independence standards. The Audit Committee s members are not professionally engaged in the practice of accounting or auditing, and they necessarily rely on the work and assurances of the Company s management and the independent registered public accounting firm. Management has the primary responsibility for the financial statements and the reporting process, including the system of internal control over financial reporting. The independent registered public accounting firm of Deloitte & Touche LLP (D&T) is responsible for performing an independent audit of the Company s consolidated financial statements in accordance with generally accepted auditing standards and expressing opinions on the conformity of those audited financial statements with United States generally accepted accounting principles, the effectiveness of the Company s internal control over financial reporting and management s assessment of the internal control over financial reporting.

The Audit Committee has: (i) reviewed and discussed with management the Company s audited financial statements for the fiscal year ended March 31, 2012; (ii) discussed with D&T the matters required to be discussed by Statement on Auditing Standards No. 61, as amended (AICPA, Professional Standards, Vol. 1, AU section 380), as adopted by the Public Company Accounting Oversight Board in Rule 3200T; (iii) received the written disclosures and the letter from D&T required by applicable requirements of the Public Company Accounting Oversight Board regarding D&T s communications with the Audit Committee concerning independence; and (iv) discussed with D&T its independence from the Company. The Audit Committee further considered whether the provision of non-audit related services by D&T to the Company is compatible with maintaining the independence of that firm from the Company. The Audit Committee has also discussed with management of the Company and D&T such other matters and received such assurances from them as it deemed appropriate.

The Audit Committee discussed with the Company s internal auditors and D&T the overall scope and plans for their respective audits. The Audit Committee meets regularly with the internal auditors and D&T, with and without management present, to discuss the results of their examinations, the evaluation of the Company s internal control over financial reporting and the overall quality of the Company s accounting.

In reliance on the reviews and discussions referred to above, the Audit Committee recommended to the Board of Directors, and the Board has approved, that the audited financial statements for the fiscal year ended March 31, 2012 be included in the Company s Annual Report on Form 10-K for filing with the SEC.

Audit Committee of the
Board of Directors

Marie L. Knowles, Chair
Andy D. Bryant
Wayne A. Budd
Jane E. Shaw, Ph.D.

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PRINCIPAL STOCKHOLDERS

Security Ownership of Certain Beneficial Owners

The following table sets forth information regarding ownership of the Company s outstanding common stock by any entity or person, to the extent known by us or ascertainable from public filings, to be the beneficial owner of more than five percent of the outstanding shares of common stock:

Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class*
T. Rowe Price Associates, Inc. 100 E. Pratt Street Baltimore, Maryland 21202	21,795,513(1)	9.2%
FMR LLC and Edward C. Johnson 3d 82 Devonshire Street Boston, Massachusetts 02109	16,235,003(2)	6.9%
Wellington Management Company, LLP 280 Congress Street Boston, Massachusetts 02210	15,139,257(3)	6.4%
BlackRock, Inc. 40 East 52nd Street New York, New York 10022	14,664,168(4)	6.2%

* Based on 236,187,328 shares of common stock outstanding as of May 31, 2012.

(1) This information is based upon a Schedule 13G/A filed with the SEC on February 9, 2012 by T. Rowe Price Associates, Inc. (Price Associates), which reports sole voting power with respect to 7,277,464 shares, sole dispositive power with respect to 21,791,963 shares, and an aggregate beneficial ownership of 21,795,513 shares. These securities are owned by various individual and institutional investors, for which Price Associates serves as investment advisor with power to direct investments and/or sole power to vote the securities. For purposes of the reporting requirements of the Securities Exchange Act of 1934, as amended, Price Associates is deemed to be a beneficial owner of such securities; however, Price Associates expressly disclaims that it is, in fact, the beneficial owner of such securities.

(2) This information is based upon a Schedule 13G/A filed with the SEC on February 14, 2012 by FRM LLC and Edward C. Johnson 3d, which reports sole voting power with respect to 1,706,836 shares and sole dispositive power with respect to 16,235,003 shares.

(3) This information is based upon a Schedule 13G/A filed with the SEC on February 14, 2012 by Wellington Management Company, LLP, which reports shared voting power with respect to 2,714,430 shares and shared dispositive power with respect to 15,139,257 shares.

(4) This information is based upon a Schedule 13G/A filed with the SEC on February 13, 2012 by BlackRock, Inc., which reports sole voting and dispositive power with respect to 14,664,168 shares.

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Security Ownership of Directors and Executive Officers

The following table sets forth, as of May 31, 2012, except as otherwise noted, information regarding ownership of the Company s outstanding common stock by: (i) all directors, each of whom is also a director nominee; (ii) each executive officer named in the 2012 Summary Compensation Table below (collectively, the NEOs); and (iii) all directors, NEOs and executive officers as a group. The table also includes shares of common stock that underlie outstanding RSUs and options to purchase common stock of the Company that either vest or become exercisable within 60 days of May 31, 2012:

Name of Individual	Shares of Common Stock Beneficially Owned(1)	Percent of Class
Andy D. Bryant	11,225(2)	*
Wayne A. Budd	20,041(2)(4)	*
Jeffrey C. Campbell	628,264(3)(4)(5)	*
John H. Hammergren	2,028,818(3)(4)(5)	*
Alton F. Irby III	71,834(2)(3)(4)	*
M. Christine Jacobs	23,459(2)	*
Paul C. Julian	805,402(3)(5)	*
Marie L. Knowles	9,342(2)	*
David M. Lawrence, M.D.	27,795(2)(3)	*
Edward A. Mueller	10,744(2)	*
Marc E. Owen	351,838(3)(5)	*
Laureen E. Seeger	19,667(3)(5)	*
Jane E. Shaw, Ph.D.	69,029(2)(4)	*
All directors, NEOs and executive officers as a group (16 persons)	4,518,747(2)(3)(4)(5)	1.9%

* Less than 1.0%. The number of shares beneficially owned and the percentage of shares beneficially owned are based on 236,187,328 shares of the Company s common stock outstanding as of May 31, 2012, adjusted as required by the rules promulgated by the SEC. Shares of common stock that may be acquired by exercise of stock options or vesting of RSUs within 60 days of May 31, 2012 and vested RSUs that are not yet settled are deemed outstanding and beneficially owned by the person holding such stock options or RSUs for purposes of computing the number of shares and percentage beneficially owned, but are not deemed outstanding for purposes of computing the percentage beneficially owned by any other person.

(1) Except as otherwise indicated in the footnotes to this table, the persons named have sole voting and investment power with respect to all shares of common stock shown as beneficially owned by them, subject to community property laws where applicable.

(2) Includes vested RSUs or common stock units accrued under the 2005 Stock Plan, Directors Deferred Compensation Administration Plan and the 1997 Non-Employee Directors Equity Compensation and Deferral Plan (which plan has been replaced by the 2005 Stock Plan) as follows: Mr. Bryant, 11,225 units; Mr. Budd, 19,941 units; Mr. Irby, 19,793 units; Ms. Jacobs, 22,459 units; Ms. Knowles, 9,342 units; Dr. Lawrence, 20,295 units; Mr. Mueller, 10,744 units; Dr. Shaw, 41,802 units; and all directors as a group, 155,601 units. Directors have neither voting nor investment power with respect to such units.

(3) Includes shares that may be acquired by exercise of stock options or vesting of RSUs within 60 days of May 31, 2012 as follows: Mr. Campbell, 559,750 shares; Mr. Hammergren, 1,434,500 shares; Mr. Irby, 21,993 shares; Mr. Julian, 805,000 shares; Dr. Lawrence, 7,500 shares; Mr. Owen, 311,250 shares; Ms. Seeger, 17,250 shares; and all directors, NEOs and executive officers as a group, 3,536,743 shares.

(4) Includes shares held by immediate family members who share a household with the named person, by family trusts as to which the named person and his or her spouse have shared voting and investment power, or by an independent trust for which the named person disclaims beneficial ownership as follows: Mr. Budd, 100 shares; Mr. Campbell, 67,532 shares; Mr. Hammergren, 590,257 shares; Mr. Irby, 1,550 shares; Dr. Shaw, 11,437 shares; and all directors, NEOs and executive officers as a group, 671,147 shares.

(5) Includes shares held under the Company s PSIP as of May 31, 2012 as follows: Mr. Campbell, 982 shares; Mr. Hammergren, 4,061 shares; Mr. Julian, 345 shares; Mr. Owen, 1,436 shares; Ms. Seeger, 1,349 shares; and all NEOs and executive officers as a group, 11,462 shares.

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EXECUTIVE COMPENSATION

COMPENSATION DISCUSSION AND ANALYSIS

EXECUTIVE SUMMARY

General

We are pleased to report that FY 2012 was another year of strong financial and operational performance for McKesson and its stockholders. Our revenues and earnings once again increased over the prior year, and we used our strong balance sheet and solid liquidity position to continue the implementation of our portfolio approach to capital deployment. Consequently, our annual and three-year financial performance exceeded the target levels set by the Compensation Committee for our executive compensation program.

Against the backdrop of superior Company performance and stockholder return, the Compensation Committee has made a number of important changes to our executive compensation program. These changes reflect the Compensation Committee s continuing commitment to refine McKesson s pay for performance philosophy, embrace contemporary practices, compete in the market for and retain executive talent, and incorporate stockholder feedback. Further, these changes are having the effect of moderating the compensation provided to our CEO, CFO and the three next most highly compensated executive officers, all of whom are listed in our Summary Compensation Table for FY 2012 (collectively, our NEOs). Consequently, FY 2012 is the second consecutive year where our financial performance was up and executive compensation was down.

Performance Results

In FY 2012, McKesson generated double-digit growth in both revenues and earnings, driven by outstanding execution of our portfolio approach to capital deployment. These results extend our track record of successfully growing revenues and earnings, which we have returned to stockholders in the form of increasing dividend payments:

* See *Appendix A* to this proxy statement for a reconciliation of diluted earnings per share from continuing operations as reported under U.S. generally accepted accounting principles (GAAP) to adjusted earnings per share (Adjusted EPS). Non-GAAP measures such as Adjusted EPS should be viewed in addition to, and not as an alternative for, financial results prepared in accordance with GAAP.

Over the last five years, we have centralized our operations and services to gain efficiencies of scale while increasing the quality of our products and services, improved operating processes using Six Sigma, introduced innovative new solutions to drive customer satisfaction, and maintained high levels of employee engagement and retention. We have also deployed approximately $13 billion of capital, including $3.6 billion in FY 2012 to:

- Reshape the organization, expand market penetration and increase earnings through reinvestment in our business;
- Pay dividends to our stockholders at rates competitive with other companies in our sector;
- Complete a series of value-creating acquisitions, including our recent purchase of the independent banner and franchise businesses of the Katz Group Canada Inc. for approximately $919 million; and

Expand and execute on our stock repurchase program.

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During FY 2012, the Company repurchased $1.9 billion of common stock, paid $195 million in dividends and made internal investments of $403 million. Each of these important accomplishments was fueled by our strong operating cash flows, which over the past five years totaled more than $9.8 billion. As a result, at the end of the most recent fiscal year we had more than $3.1 billion in cash and cash equivalents, which we believe will serve as a catalyst for our future growth.

The impact of our recent operational and financial success on FY 2012 awards to our NEOs is detailed below under Annual Compensation and Long-term Compensation. For a comprehensive discussion of our financial results, please refer to our Annual Report on Form 10-K for the fiscal year ended March 31, 2012, filed with the SEC on May 2, 2012.

Total Stockholder Return

Mr. Hammergren was appointed sole chief executive officer of McKesson in April 2001. Over the years, he has assembled a high-performing executive team that has driven McKesson to tremendous growth and success, which has in turn translated into superior value for our stockholders. Our executive compensation program is designed to incentivize execution of our strategy, and our experienced and long-tenured management team has a steady track record of delivering results and superior returns to our stockholders.

The table below displays our total stockholder return over the last five fiscal years, indexed against the S&P 500 and the Value Line Healthcare Sector Index, and the five-year trend of compensation provided to our NEOs. Total stockholder return assumes $100 invested at the close of trading on March 31, 2007 and the reinvestment of dividends when paid. For purposes of this display, we have used compensation figures disclosed in Summary Compensation Tables required under SEC rules, minus pension accrual because we do not believe the pension accrual is part of direct compensation. This display demonstrates the delivery of long-term value to McKesson stockholders and how the Compensation Committee s recent refinements to our program are affecting executive compensation trends.

Total Stockholder Return and NEO Compensation

Chief Executive Officer

Average Other NEOs

Company/Index	3/31/2007	3/31/2008	3/31/2009	3/31/2010	3/31/2011	3/31/2012
McKesson Corporation	100	89.81	60.73	114.92	139.72	156.68
Value Line Healthcare Sector Index	100	94.52	72.44	100.35	119.57	136.05
S&P 500 Index	100	94.92	58.77	88.02	101.79	110.49

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Changes to the Program

The following highlights significant events and developments affecting our executive compensation program for FY 2012 and FY 2013:

Our CEO, Mr. Hammergren, relinquished his right to be paid a golden parachute excise tax gross-up, and his potential cash severance pay for a termination in connection with a change in control has been significantly reduced.

The Compensation Committee added new financial metrics to our executive compensation program to enhance the alignment between our program and the Company s financial and operating performance, which we believe will ultimately drive share price performance and investors return. We currently use the following metrics:

Financial Performance Metric	Definition
Adjusted EPS	Earnings per diluted share from continuing operations, excluding acquisition-related expenses, amortization of acquisition-related intangible assets and certain litigation reserve items
Adjusted EBITDA	Adjusted earnings before interest income, interest expense, taxes, depreciation and amortization
Adjusted ROIC	Adjusted return on invested capital
Long-term Earnings Growth	Compound annual growth rate of adjusted earnings per diluted share measured over a three-year performance period
Adjusted OCF	Operating cash flow adjusted for payments for certain litigation reserve items

We eliminated the individual modifier from our performance restricted stock unit program for all of our executive officers so that the delivered value of these awards is now based solely on the financial performance of the Company.

We moderated our executive officers future potential payouts under our cash long-term incentive plan by reducing the maximum opportunity by 33% and reducing the target awards by 5%.

We extended our policy prohibiting new excise tax gross-up provisions to cover all agreements with executive officers.

In response to stockholder feedback, we eliminated General Electric Company and Oracle Corporation from our compensation peer group.

Continuing Executive Compensation and Governance Practices

The most recent modifications to our executive incentive program described above continue a multi-year process undertaken by the Compensation Committee to evolve our continuing executive compensation practices. These actions and continuing practices are highlighted below.

We are committed to aligning pay with stockholder interests.

We pay for performance. Base salaries for our NEOs average approximately 11% or less of their total annual compensation and the great majority of their direct compensation is tied to financial and strategic performance.

Nearly 70% of our NEOs target direct compensation consists of equity awards.

Our NEOs equity incentive awards vest over four years.

Our equity compensation vests in connection with a change in control only if the employee also incurs a qualifying termination of employment a so-called double-trigger vesting provision.

We have reduced our equity overhang by reducing stock option grants and adding restricted stock units to the program.

In recognition of changing market practices, we have evolved our executive compensation program over the last few years by including multiple financial performance metrics.

Our performance metrics align executive pay with the implementation of our portfolio strategy for growth.

NEO compensation as reported in our 2012 Summary Compensation Table is down an average of more than 9% from 2011, and our CEO s total compensation as reported in the same table decreased by more than 13% from 2011.

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We are committed to sound governance practices.

The Compensation Committee engages independent legal counsel and an independent compensation consultant.

The Compensation Committee regularly reviews tally sheets and other reports detailing all components of our executive compensation program, including projected potential severance and change in control payouts.

We perform a robust annual review of all of our incentive programs to determine whether they present a material risk to the Company.

We will not enter into any new agreement with an executive officer providing for a golden parachute excise tax gross-up.

We have not paid a tax gross-up on any executive perquisite since 2008.

We froze our executive pension plan and executive life insurance plan to new participants.

We discontinued our executive medical plan and executive short-term disability plan.

We will not adopt or enter into any new supplemental death benefit arrangement for an executive officer which is not provided to employees generally, unless it is approved by McKesson s stockholders pursuant to an advisory vote.

We adopted a robust set of guidelines on executive stock ownership, which all of our NEOs have satisfied.

We adopted a rigorous compensation clawback and recoupment policy that is more stringent than required under applicable law.

We discontinued the practice of entering into employment agreements with our executive officers.

We will not reprice stock options without stockholder approval.

We prohibit all directors and employees from engaging in hedging transactions through the use of certain derivatives, such as put and call options involving Company securities.

Say on Pay and Stockholder Outreach

We have a long-standing practice of engaging in dialogue with our stockholders about various corporate governance topics. Insights we have gained from these discussions over the years have been helpful to our Board and its Compensation Committee as they consider and adopt policies that affect our employees, including our NEOs.

Last year, we held our first advisory vote to approve NEO compensation, commonly known as say on pay, as well as our first advisory vote on the frequency of future say on pay votes. Of the shares present and entitled to vote, nearly seventy percent (70%) were voted in support of the advisory say on pay proposal, and nearly ninety-two percent (92%) were voted with the Board s recommendation that we should hold future advisory say on pay votes annually. While we are pleased that a significant majority of our stockholders supported our NEO compensation, we also acknowledge that approximately thirty percent (30%) of the shares present and entitled to vote did not support the advisory say on pay proposal.

In anticipation of the advisory say on pay vote, our Board and management team embarked on a multi-pronged effort to gather feedback from key stakeholders regarding our executive compensation program. This included telephonic and in-person discussions with individual and institutional stockholders, review of written correspondence submitted by individual and institutional stockholders to the Board and management, internal discussions with employees, analysis of market practices at peer companies, advice from the Compensation Committee s independent compensation consultant and legal counsel, discussions with proxy advisory services and corporate governance research firms, and review of media reports regarding our executive compensation program and the Compensation Committee s decisions. Most stockholders we spoke to acknowledged our financial and operational performance and our long-tenured senior management team, and spoke appreciatively of the recent changes we made to our governance practices and executive compensation program. Some stockholders expressed concern regarding our use of a single financial metric in multiple incentive plans, and a few added that even with our recent changes, they expect continued refinement to our governance practices and executive compensation program.

As a result of this feedback, we significantly changed the architecture of our FY 2012 executive compensation program by adding new financial metrics. We eliminated individual performance as a modifier of executive officer awards under our performance restricted stock unit program. We also moderated future potential payouts to our executive officers under our cash long-term incentive plan by reducing the maximum payout by 33% and reducing target awards by 5%. Earlier this year, our CEO relinquished his right to be paid a golden parachute tax gross-up and his potential cash severance for a termination in connection with a change in control was significantly reduced. Finally, we extended our policy prohibiting new rights to excise tax gross-ups to cover all new agreements (or materially amended agreements) with our executive officers. These program design changes and the relinquishment of significant rights by our CEO were described in greater detail above under the subheading, Changes to the Program.

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Although the say on pay vote is non-binding and generally relates to compensation decisions that have already been made, the Compensation Committee has considered, and will continue to consider, the outcome of this vote each year when setting compensation policies and making compensation decisions regarding our NEOs.

Compensation Philosophy and Implementation

McKesson fosters a performance-driven culture by requiring executives to surpass target financial goals, and to identify the ways each executive contributed to those results, in order to receive compensation above his or her target amount. We have designed our executive compensation program to advance our objective of increasing stockholder returns and sustained value creation without promoting excessive risk-taking.

In keeping with our pay for performance culture, a large percentage of our executive compensation is tied to long-term performance, and much of our long-term compensation program is based on the value of our common stock. This structure aligns the interests of our executives with those of our long-term stockholders.

The graphics below illustrate the mix of fixed and variable target direct compensation we provide to our NEOs. These proportions have remained generally consistent year-over-year.

Direct Compensation Elements

McKesson s executive compensation program provides for a mix of base salary, annual bonus and long-term incentive awards and imposes rigorous guidelines for minimum share ownership.

Our approach to delivering direct compensation is to provide market-competitive target compensation levels. The amount ultimately realized by our NEOs under our program is based on McKesson s performance over time and any increases or decreases in share price. We take a long-term approach to compensation, just as we take a long-term approach to building stockholder value.

Our direct compensation elements for FY 2012 are as follows:

Element	Type	Alignment with Stockholder Value Creation
Base salary	Fixed	Attracts and retains high performing executives by providing market-competitive fixed pay
Annual performance-based cash incentive	Variable	Drives company-wide, business unit and individual performance Focuses efforts on growing earnings, profitability and cash flow as well as delivering on strategic business goals
Long-term performance-based incentives consisting of performance restricted stock units, stock options and cash	Variable	Aligns executives interests with those of stockholders Motivates executives to deliver sustained long-term growth in McKesson s share price Size and payouts of awards are based on business and individual performance as well as potential for future contributions

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Performance Objectives

The metrics approved by the Compensation Committee in our short- and long-term incentive program for FY 2012, and the rationales for choosing the metrics, are as follows:

Incentive Program	Type	Financial Metrics	Rationale for Selection
Management Incentive Plan (MIP)	Annual (cash)	Adjusted EPS	Most relevant to share price valuation and stockholder expectations
		Adjusted EBITDA	Focuses on operational performance
		Individual modifier	Assesses performance against individual goals
Long-Term Incentive Plan (LTIP)	Long-term (cash)	Long-term Earnings Growth	Focuses on long-term return and the achievement of multi-year objectives
		Adjusted OCF	Focuses on efficient management of working capital and cash generation which, in turn, creates stockholder value
Performance Restricted Stock Units (PeRSUs)	Long-term (equity)	Adjusted EPS	Most relevant to share price valuation and stockholder expectations
		Adjusted ROIC	Measures capital efficiency and productive deployment of capital
Stock Options	Long-term (equity)	Share price	Most closely ties realized compensation to investors focus on increasing share price

At the beginning of FY 2012, the Compensation Committee added additional metrics to our program to enhance the alignment between our program and the Company s financial and operating performance, and to further mitigate any potential risk that a single-metric program may have presented to the Company. In selecting these metrics, the Compensation Committee analyzed historical trends, the incentive plan design features and performance of comparable U.S. companies, analyst expectations and investor feedback. Among our investors, we found EPS, the financial metric we have historically used, to be the universally tracked metric, with EBITDA as the second most prevalent metric. After EPS and EBITDA were a group of metrics focused on the productive deployment of capital (*i.e.,* ROIC, ROE (return on equity), etc.) as well as cash flow per share metrics. The Compensation Committee determined to adopt those metrics most commonly tracked by investors as well as metrics used by our peers in their executive compensation plans, with the ultimate goal being to focus management on the performance factors that complement our portfolio approach to capital deployment.

Compensation Peer Group

The Compensation Committee oversees the design of our executive compensation program and regularly evaluates the program against competitive practices, legal and regulatory developments and corporate governance trends. The Compensation Committee has worked with its independent compensation consultant to develop a compensation peer group of companies that it believes best represents the group of companies against which the Company competes for executive talent (our Compensation Peer Group). A table displaying our Compensation Peer Group is provided below under Use and Selection of Our Compensation Peer Group. The Compensation Committee does not advocate a specific percentile relationship of target compensation to market compensation; however, the data derived from our Compensation Peer Group is used to provide context for the Compensation Committee s decision-making process.

Talent Attraction & Retention

It is critical to the Company s long-term success and growth that our businesses are managed by highly capable leaders with the experience, skills, diversity and dedication to oversee a growing organization in a highly regulated industry and changing global environment. We have

designed our executive compensation program to attract and retain high-performing managers and to motivate these managers to increase the market value of our stock over the long term. In support of these principal objectives, our executive compensation program is designed to:

- Provide base salaries, retirement and other benefits and perquisites that are competitive with those provided by other companies with whom we compete for executive talent;

- Pay bonuses that reward our executives for meeting or exceeding our financial, operational and strategic goals;

- Grant equity-based compensation that will motivate them to improve our long-term performance and specifically, to increase the market value of our stock price over time, in addition to helping retain those executives; and

- Motivate our executives to improve their individual performance.

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HOW WE MAKE COMPENSATION DECISIONS

Executive Officer Compensation Oversight

The Compensation Committee has responsibility for overseeing all forms of compensation for our executive officers, including our NEOs. For FY 2012, our NEOs and their respective titles were as follows:

- John H. Hammergren, *Chairman of the Board, President and Chief Executive Officer*;
- Jeffrey C. Campbell, *Executive Vice President and Chief Financial Officer*;
- Paul C. Julian, *Executive Vice President and Group President*;
- Marc E. Owen, *Executive Vice President, Corporate Strategy and Business Development;* and
- Laureen E. Seeger, *Executive Vice President, General Counsel and Chief Compliance Officer.*

Role of the Independent Compensation Consultant and Legal Counsel

In FY 2012, the Compensation Committee continued to directly employ its own independent compensation consultant, Compensation Strategies, Inc., and its own independent legal counsel, Gunderson Dettmer Stough Villeneuve Franklin & Hachigian, LLP. The independent compensation consultant s duties include the following:

- reviewing our total compensation philosophy, Compensation Peer Group, and target competitive positioning for reasonableness and appropriateness;
- reviewing our overall executive compensation program and advising the Compensation Committee on evolving best practices;
- providing independent analyses and recommendations to the Compensation Committee on executive officers compensation, and compensation proposals submitted by management to the committee for its approval; and
- reviewing the Compensation Discussion and Analysis for our proxy statement.

The independent legal counsel s duties include providing assistance interpreting the various rules and regulations related to our executive compensation program, and reviewing the Compensation Discussion and Analysis for our proxy statement.

As outlined in its charter, the Compensation Committee has final authority to retain and terminate its independent compensation consultant and legal counsel, and it must evaluate their qualifications, performance and independence annually. The compensation consultant and legal counsel interact directly with members of the Company s management only on matters under the Compensation Committee s oversight and with its knowledge and permission. To ensure that it receives independent and unbiased advice and analysis, the Compensation Committee has also adopted a formal independence policy that must be certified annually by its compensation consultant and legal counsel. Finally, the compensation consultant and legal counsel report directly to the Compensation Committee and do not perform any services for management. However, as noted earlier, Compensation Strategies, Inc. also provides consulting services to the Governance Committee in the area of director compensation.

Use and Selection of Our Compensation Peer Group

In order to attract and retain highly qualified individuals, a key objective of our executive compensation program is to ensure that the total compensation package for our executive officers is competitive with the companies against which we compete for executive talent. To that end, the Compensation Committee s independent compensation consultant annually develops information that captures from a diverse group of public companies the levels of total compensation and individual components of direct compensation (base salary and annual and long-term incentive potential) for executives having duties and responsibilities similar to the Company s executives. Information sources used by the independent compensation consultant include the Hewitt Associates Total Compensation Database and compensation information published by other public companies. From this larger sampling, the Compensation Committee and our independent compensation consultant derive a list of peer group companies against which the Company historically competes for executive talent. We believe this diverse selection of peer group companies, as identified in the chart below, provides us with a better understanding of the evolving and competitive marketplace for executive talent.

The Compensation Committee uses data derived from our Compensation Peer Group as a guideline to assist the committee in its decisions about overall compensation, the elements of compensation, the amount of each element of compensation and the relative competitive landscape of our executive compensation program. Although the Compensation Committee uses various metrics derived from our Compensation Peer Group to provide context for its own determinations and strategies, it does not advocate a specific percentile relationship of target compensation to market compensation derived from the peer group; that is, it does not strive for any individual compensation component or compensation in the aggregate to be at any specific level (for instance, at the 75th percentile). Rather, using the 50th and 75th percentiles as reference points, the Compensation Committee reviews the mix of our compensation components with respect to fixed versus variable, annual versus long-term and cash versus

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equity-based pay in order to set target direct compensation. Ultimately, due to a number of variables including share price, individual performance and company performance, total direct compensation delivered to our executive officers may be higher or lower than the 50th or 75th percentiles of our Compensation Peer Group.

As part of its annual review process, the Compensation Committee and its independent compensation consultant endeavor to design our Compensation Peer Group such that the addition or removal of any single company would not have a material impact on the survey results. Revenue sizes of our Compensation Peer Group companies vary considerably. To adjust for these differences, regression analysis is used to determine a size-adjusted market compensation level.

The following list of companies represents our Compensation Peer Group as utilized by the Compensation Committee at its May 2011 meeting, during which it determined FY 2012 executive compensation:

Company Name	Revenue*	Company Name	Revenue*
Abbott Laboratories	38.9	Johnson & Johnson	65.0
Aetna Inc.	33.8	Eli Lilly and Company	24.3
AmerisourceBergen Corporation	80.2	Medco Health Solutions, Inc.	70.1
Amgen Inc.	15.6	Medtronic, Inc.	15.9
Automatic Data Processing, Inc.	9.9	Merck & Company, Inc.	48.0
Baxter International Inc.	13.9	Omnicare, Inc.	6.2
Becton, Dickinson and Company	7.8	Pfizer Inc.	67.4
Bristol-Myers Squibb Company	21.2	Rite Aid Corporation	26.1
Cardinal Health, Inc.	102.6	Safeway Inc.	43.6
Computer Sciences Corporation	16.0	Stryker Corporation	8.3
Covidien Public Limited Company	11.6	Sysco Corporation	39.3
CVS Caremark Corporation	107.1	Thermo Fisher Scientific, Inc.	11.7
Express Scripts, Inc.	46.1	UnitedHealth Group Inc.	101.9
FedEx Corporation	39.3	Walgreen Co.	72.2
Ingram Micro Inc.	36.3	WellPoint, Inc.	60.7
International Business Machines Corporation	106.9	**McKesson Corporation**	**122.7**

* Financial results are stated in billions for the most recently completed fiscal year as publicly reported by each company listed above as of May 31, 2012.

Having removed General Electric Company and Oracle Corporation from our Compensation Peer Group for FY 2012 in response to stockholder feedback, the Compensation Committee determined at its April 2012 meeting not to make changes to our FY 2013 Compensation Peer Group other than to remove Medco Health Solutions Inc. as a consequence of its April 2012 acquisition by Express Scripts, Inc.

Our Compensation Review and Determination Process

The Compensation Committee has responsibility for setting performance targets and payout scales for each of our executive officers. While performance targets and payout scales are initially developed by senior management, and are informed by the one-year operating plan and three-year strategic plan reviewed with the Board, the Compensation Committee in its sole discretion approves, modifies or amends management s target and payout scale recommendations. When reviewing these recommendations, the Compensation Committee generally selects performance targets that are consistent with the operating and strategic plans reviewed with the Board and with the information routinely communicated to our employees or investors by management. Differences in the NEOs target compensation occur because the Compensation Committee considers a number of factors when evaluating their target annual and long-term compensation in relation to the Compensation Peer Group data, including job performance, skill set, prior experience, the executive s time in his or her position and/or with the Company, internal consistency regarding pay levels for similar positions or skill levels within the Company, external pressures to attract and retain talent, and general market conditions.

A detailed annual performance review process begins in April with all members of the Company s senior management preparing a written analysis of their actual performance against the goals established for the prior fiscal year, as well as their performance goals for the upcoming fiscal year. These individual performance goals are established by senior management with reference to the Company s annual budget and strategic planning processes. Each member of senior management then reviews with our CEO his or her performance goals, as well as the executive s performance against the goals established for the prior fiscal year. Each executive is then evaluated on his or her commitment to the Company s ICARE principles, which serves as a guide to all our employees enterprise-wide. These principles are integrity, customer first, accountability, respect and excellence. ICARE is the cultural foundation of the Company, and the principles unify the Company and guide individuals behavior toward each other, customers, vendors and other stakeholders.

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Our CEO, in consultation with the Compensation Committee s independent compensation consultant and the Executive Vice President, Human Resources, then develops compensation recommendations for each executive officer. Factors that our CEO weighs in making individual target compensation recommendations include: (i) the findings from his or her performance review; (ii) value of the job in the marketplace; (iii) relative importance of the position within our executive ranks; (iv) individual tenure and experience; and (v) individual contributions to the Company s results. Early in the fiscal year, the Board conducts a performance review of our CEO on the same basis described above with respect to the CEO s review of other executive officers. In advance of this review, our CEO distributes to the Board a written analysis of his accomplishments keyed to the business and individual goals established for the prior fiscal year. At the Board meeting, our CEO presents his individual performance results for the prior fiscal year and recommends his individual goals for the new fiscal year, and responds to any questions that may arise. Upon completion of his performance review, the Board discusses in executive session our CEO s performance for the prior fiscal year and approves, modifies or amends his individual goals for the new fiscal year.

At its May meeting, in connection with determining incentive payouts for the prior fiscal year and establishing goals for the current performance periods, the Compensation Committee reviews and evaluates compensation matters for all executive officers, including our CEO. Over the course of the year, in its review of compensation for all of our executive officers, the Compensation Committee reviews tally sheets, which include the compensation that is proposed for the upcoming fiscal year and compensation delivered for the prior year or over the past several years, a compilation of the outstanding and as yet unearned cash and equity awards for each officer, and a display detailing the elements of current compensation and estimated benefits on separation from service under various circumstances, including in connection with a change in control. The Compensation Committee finds tools like tally sheets and displays of total holdings helpful in its analysis of the Company s executive compensation program, but in determining the specific levels of compensation, the Compensation Committee is generally more focused on the elements of direct compensation and the measurement of these elements against similarly situated executives in the Compensation Peer Group. Determinations of CEO compensation are made in executive session with input from the Compensation Committee s independent compensation consultant.

Finally, in October of each year, the Compensation Committee conducts a detailed review of all elements of executive compensation, including a review of tally sheets regarding our NEOs and other executive officers. This second set of tally sheets displays the elements of current compensation and estimated benefits on separation from service due to voluntary and involuntary termination and termination in connection with a change in control with respect to the then-current fiscal year. At the same October meeting, management updates the Compensation Committee on actual performance against the pre-established goals for all outstanding incentive compensation programs.

EXECUTIVE OFFICER COMPENSATION ELEMENTS

The Compensation Committee s overall objective is to provide NEO direct compensation at levels that are competitive with similarly situated executives within our Compensation Peer Group. Each NEO s target annual compensation (base salary and MIP) is reviewed in relation to the 50th percentile for that position within our Compensation Peer Group, and each NEO s target long-term compensation (LTIP and equity) is reviewed in relation to the 50th and 75th percentiles of our Compensation Peer Group. Our pay for performance program is designed to drive financial and operational performance well above the pre-established targets.

The basic elements of our executive compensation program are: annual compensation, long-term compensation, benefits and perquisites, and severance and change in control benefits. Our annual and long-term compensation elements constitute direct compensation, and are comprised of four components: base salary, annual performance-based bonus, long-term performance-based bonus, and equity awards, currently comprised of stock options and restricted stock units.

An executive s target compensation is based on his or her level of experience, his or her individual performance, and the performance of the Company. As an executive s ability to impact financial performance increases, so does the proportion of his or her at-risk compensation. In addition, target long-term compensation grows proportionately as job responsibility increases.

In addition to direct compensation, we provide our executive officers with employee benefits and certain perquisites, along with severance and change in control benefits, so that we can attract and retain talented executives to the degree such benefits are market competitive, or to the degree that such benefits are in the best interest of the Company and its stockholders.

During the process of determining the composition of each NEO s target direct compensation package, the Compensation Committee evaluates many factors, including the following:

- alignment of executive and stockholder interests in achieving long-term growth in stockholder value;

ensuring that exceptional rewards are attained only for exceptional performance;
the value of compensation packages being significant enough to encourage a high-performing executive s continued full-time commitment to the Company; and
the total cost of compensation, including estimated future payouts for performance-based awards, and affordability of that cost to the Company.

The allocation between annual and long-term compensation, and the determination of performance goals for our various programs, is also based on the Compensation Committee s evaluation of each NEO s skill and experience, and in response to market data derived from the Company s Compensation Peer Group as reviewed by the Compensation Committee with its independent compensation consultant.

Annual Compensation

Annual compensation is delivered in cash with a substantial variable portion being at-risk and contingent on the successful accomplishment of pre-established performance goals. We believe it is important to have at-risk compensation that can be focused on short-term Company and individual goals.

Base Salary. Base salary for executive officers is assessed the same way base salary is determined for all employees base salary is reviewed in relation to the 50th percentile for that position within the Company s Compensation Peer Group. Base salaries for our NEOs are reviewed in May of each year. In May 2011, the Compensation Committee approved FY 2012 base salary increases for all NEOs, effective immediately, ranging from 1.9% to 4.3% for all NEOs, except that our CEO s base salary was left unchanged by the Compensation Committee upon his request. At its May 2012 meeting, following consideration of all the components of direct compensation, the Compensation Committee determined to maintain our NEOs base salaries at their current levels.

Annual Incentive. The Management Incentive Plan (MIP) is our annual cash incentive program with payment conditioned on the achievement of individual and Company financial performance goals. The MIP, like base salary, is intended to deliver short-term cash incentive compensation in reference to the 50th percentile of our Compensation Peer Group when performance meets the pre-determined target levels.

In May 2011, the Compensation Committee selected Adjusted EPS, Adjusted EBITDA and individual performance as MIP modifiers for the fiscal year ending March 31, 2012. The Compensation Committee utilized Adjusted EPS as the primary financial performance measure because it is a key metric used by management to direct and measure the Company s business performance, and the basis upon which we communicate forward-looking financial information to the investment community. Moreover, we believe that Adjusted EPS measures are clearly understood by both our employees and stockholders, and that incremental Adjusted EPS growth leads to the creation of long-term stockholder value. The Compensation Committee selected Adjusted EBITDA as the secondary metric for the MIP to focus management on operational performance. The Compensation Committee has the discretion to further adjust the actual MIP award amount by an individual performance modifier that reflects the result of the NEO s performance against non-financial objectives and initiatives. These include but are not limited to the following metrics: (i) employee engagement, as measured annually and compared against norms established by global high performing companies; and (ii) customer satisfaction, as measured annually.

For FY 2012, our NEOs were eligible for MIP target award opportunities that ranged from 80% to 150% of their base salaries. The actual MIP award delivered to each NEO may range from zero to 300% of the target award amount. The table below shows our Adjusted EPS and Adjusted EBITDA goals and their weighting, and demonstrates the calculation of the actual MIP award. As is the case for all of the Company s performance-based payout scales, when a result falls between the above-identified reference points, the modifier is adjusted ratably along the scale. The dollar values of threshold, target and maximum payouts for the FY 2012 MIP are displayed below in the 2012 Grants of Plan-Based Awards Table.

75% of MIP		25% of MIP	
Payout	Adjusted EPS	Payout	Adjusted EBITDA (in millions)
200%	$6.58	200%	$3,184
175%	$6.48	175%	$3,135
150%	$6.37	150%	$3,086
125%	$6.27	125%	$3,036
100%	$6.09	100%	$2,948
75%	$5.91	75%	$2,860
50%	$5.72	50%	$2,771

Our MIP program for FY 2012 paid our NEOs at 174% 188% of the target award based on a combined Adjusted EPS of $6.38 per diluted share, Adjusted EBITDA of $2,882 million, and an individual modifier ranging from 130% to 140%.

In May 2012, the Compensation Committee selected Adjusted EPS, Adjusted EBITDA and individual performance as MIP modifiers for the fiscal year ending March 31, 2013. The MIP financial goals selected by the Compensation Committee for FY 2013 are consistent with the guidance published by the Company on April 30, 2012, which disclosed a projected Adjusted EPS range of $7.05 to $7.35 per diluted share. We believe that the financial performance goals for a FY 2013 MIP target cash

award can be characterized as ambitious but attainable, meaning that based on historical performance this payout level is not assured but can reasonably be anticipated, while equally providing strong motivation for executives to strive to exceed the financial goals in a way that balances short- and long-term stockholder value creation. For FY 2013, our NEOs are eligible for MIP target cash award opportunities of 80% to 150% of their base salaries, which equate to $2,520,000, $819,850, $1,171,500, $544,800, and $548,800 for each of Messrs. Hammergren, Campbell, Julian and Owen and Ms. Seeger, respectively.

Long-term Compensation

We believe that a significant portion of direct compensation for executive officers should be contingent on delivering long-term value to all stockholders. We also believe that long-term compensation is a critical component of any executive compensation program because of the need to foster a long-term focus on the Company s financial results. Long-term compensation is an incentive tool that management and the Compensation Committee use to align the financial interests of executives and other key contributors to sustained stockholder value creation.

The Company s long-term direct compensation program for NEOs includes three opportunities: namely, a three-year cash incentive program (our LTIP), an annual stock option award and an annual award of performance restricted stock units, referred to as PeRSUs. We believe retention value is generated by the three-year performance cycle under our LTIP, and by the vesting requirements of equity awards.

The Compensation Committee reviews target long-term compensation for NEOs in reference to the 50th and 75th percentiles of our Compensation Peer Group. The targeted long-term compensation levels established in May 2011 for the FY 2012 and FY 2012 FY 2014 performance periods were consistent with the Compensation Peer Group reference points selected by the Compensation Committee.

Cash. The cash portion of the Company s long-term incentive compensation program, the LTIP, provides incentive for performance against the Company s long-term strategic plan that is regularly reviewed with the Board. Awards under the LTIP are earned over a three-year performance cycle, and a new three-year cycle with new target incentives and performance goals begins each fiscal year. Accordingly, this portion of our program has three, three-year performance cycles running concurrently. Payment under the LTIP is based solely on corporate financial performance.

The performance goals established for the FY 2010 FY 2012 LTIP performance period, which ended March 31, 2012, were (i) for 75% of the award, cumulative earnings per diluted share adjusted for certain litigation reserve items and acquisition related expenses (Cumulative EPS) of $13.23, and (ii) for 25% of the award, cumulative operating cash flow adjusted for payments for certain litigation reserve items (Cumulative Adjusted OCF) of $4,911 million. The table below shows our Cumulative EPS and Cumulative Adjusted OCF goals adopted in May 2009 and their weighting, and demonstrates the calculation of the final LTIP award. As with all of the Company s performance-based payout scales, when a result falls between the above-identified reference points, the modifier is adjusted ratably along the scale.

75% of LTIP		25% of LTIP	
Payout	Cumulative EPS	Payout	Cumulative Adjusted OCF (in millions)
300%	$14.29	300%	$6,384
250%	$14.02	250%	$6,016
200%	$13.76	200%	$5,648
150%	$13.50	150%	$5,279
100%	$13.23	100%	$4,911
50%	$12.17	50%	$2,947
0%	$11.11	0%	$ 982

The actual three-year results for the FY 2010 FY 2012 performance period were cumulative EPS of $15.30 per diluted share and Cumulative Adjusted OCF of $7,935 million. Therefore, at its May 2012 meeting, the Compensation Committee approved a payout for the FY 2010 FY 2012 LTIP at 300% of the target award in accordance with the payout scale adopted in May 2009.

At its May 2012 meeting, following its review of all components of direct compensation and market data derived from our Compensation Peer Group, the Compensation Committee determined to decrease by 5% each NEO s target value for the upcoming LTIP performance period. Accordingly, FY 2013 FY 2015 LTIP target values of $2,565,000, $641,000, $1,306,000, $380,000 and $380,000 were approved for each of Messrs. Hammergren, Campbell, Julian and Owen and Ms. Seeger, respectively. Consistent with its determination in May 2011 to reduce the LTIP opportunity for our executive officers, these awards may not exceed 200% of the target award.

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For the performance period FY 2013 FY 2015, the Compensation Committee selected performance goals that are consistent with the FY 2013 guidance published by the Company on April 30, 2012, and were set in reference to the three-year strategic plan reviewed by the Board. These LTIP payouts will be conditioned on achievement of compound annual growth rate of the Company s adjusted earnings per diluted share measured over the three-year performance period (Long-term Earnings Growth) and Adjusted OCF measured over the three-year performance period. These criteria are weighted 75% for Long-term Earnings Growth and 25% for three years Adjusted OCF. We believe that the Long-term Earnings Growth and Adjusted OCF goals for a FY 2013 FY 2015 LTIP target award can be characterized as challenging and difficult to achieve, but attainable with significant effort and skill on the part of the executive officer participants. The FY 2013 FY 2015 LTIP target values were selected by the Compensation Committee based on its allocation of long-term compensation, evaluation of each NEO s skill and experience, and in response to market data derived from our Compensation Peer Group as reviewed by the Compensation Committee with its independent compensation consultant. The Compensation Committee uses a goal based on Adjusted OCF under the LTIP in order to focus management on generation of cash and efficient management of working capital. The selection of Long-term Earnings Growth as a performance goal reflects the desire to focus management on the Company s long-term return to our stockholders.

Performance Restricted Stock Units. PeRSUs are awards conditioned on the achievement of Company performance goals, which after completion of a one-year performance period, are converted into RSUs that vest in full after completion of the fourth year. The Company s use of PeRSUs focuses executives attention on annual financial goals and stock price appreciation. Beginning with FY 2012 awards, we eliminated all non-financial modifiers in our PeRSU program for our executive officers, with the intent of further aligning the interests of our executive officers with the goals of our stockholders.

PeRSU target award opportunities are set at the beginning of each fiscal year. The FY 2012 PeRSU target award opportunities for each of our NEOs is provided in the 2012 Grants of Plan-Based Awards Table below, and the corresponding aggregate grant date fair value of these award opportunities is reflected in the 2012 Summary Compensation Table below.

In May 2011, the Compensation Committee approved a PeRSU performance target for FY 2012 of Adjusted EPS of $6.09, with Adjusted EPS results to be further modified by a multiplier based on a target Adjusted ROIC of 13.9%. The table below shows our FY 2012 Adjusted EPS goals and the range of Adjusted ROIC adjustments to be applied. The Compensation Committee included an Adjusted ROIC multiplier in the PeRSU program to drive the investment of capital, but determined to limit the adjustment, both on the upside and downside, because calculation of Adjusted ROIC is susceptible to significant swings based on one-time and/or unexpected events.

Payout	Adjusted EPS
200%	$6.70
150%	$6.39
100%	$6.09
90%	$5.60
80%	$5.18
70%	$4.69
60%	$4.26

Multiplier	Adjusted ROIC
110%	³ 15.1%
105%	14.5%
100%	13.9%
95%	13.3%
90%	£ 12.7%

Our PeRSU program for FY 2012 paid our NEOs at 153% of the target award based on a combined Adjusted EPS of $6.38 per diluted share and an Adjusted ROIC of 14.3%. Accordingly, at its May 2012 meeting, the Compensation Committee awarded each of Messrs. Hammergren, Campbell, Julian and Owen and Ms. Seeger a total of 157,590, 58,140, 87,210, 29,070, and 36,720 RSUs, respectively.

In May 2012, the Compensation Committee once again selected Adjusted EPS and Adjusted ROIC as PeRSU performance criteria for the PeRSU program for the fiscal year ending March 31, 2013. Similar to the FY 2013 FY 2015 LTIP, we believe that the Adjusted EPS and Adjusted ROIC goals for a FY 2013 PeRSU target award can be characterized as challenging and difficult to achieve, but attainable with significant effort and skill on the part of the executive officer participants. At its May 2012 meeting, following its review of all components of direct compensation and market data derived from our Compensation Peer Group, the Compensation Committee established a FY 2013 PeRSU target award opportunity of 94,000, 35,000, 52,000, 16,000, and 22,000 RSUs for each of Messrs. Hammergren, Campbell, Julian and Owen and Ms. Seeger, respectively.

Stock Options. Since stock option awards provide value to the holder only if the Company s stock price appreciates, the use of such incentives directly aligns the interests of our executives and stockholders. Stock option grants are awarded each fiscal year at the May meeting of the Compensation Committee. The determination of the size of stock option awards made to our NEOs is

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made in the Compensation Committee s discretion and judgment as to what is appropriate in light of all of the circumstances, including the balance of cash and equity in our annual and long-term incentive plans, our strategic and operational objectives, our stock price, the responsibilities of our NEOs, a review of similar grants made at companies in our Compensation Peer Group, and such other factors as the Compensation Committee deems relevant. Stock options generally vest in four equal annual installments over a four-year period and have a seven-year term. At its May 2011 meeting, the Compensation Committee awarded a stock option to each of Messrs. Hammergren, Campbell, Julian and Owen and Ms. Seeger for 301,000, 111,000, 167,000, 57,000, and 69,000 shares, respectively.

At its May 2012 meeting, the Compensation Committee awarded a stock option to each of Messrs. Hammergren, Campbell, Julian and Owen and Ms. Seeger for 298,000, 110,000, 165,000, 50,000, and 69,000 shares, respectively.

Other Compensation and Benefits

The Company provides a broad array of benefits to all employees that are comparable to those offered by other employers in our industry and geographic footprint, including a competitive suite of health and life insurance and retirement benefits. In addition, our employees are eligible to participate in the McKesson Foundation s Matching Gifts Program. Under this program, employees gifts to schools, educational associations or funds, and other public charitable organizations are eligible for a match by the foundation of up to $2,500 per employee for each fiscal year. A limited number of additional benefits are also provided to executive officers because we believe that it is customary to provide such benefits, or otherwise in the best interest of the Company and its stockholders. In providing such benefits, both management and the Compensation Committee determined that these items are appropriate for the attraction and retention of executive talent. In addition to the discussion of benefits below, the compensation associated with these items is described in footnote (5) to the 2012 Summary Compensation Table, accompanying the column entitled All Other Compensation.

The Company has two benefit plans under which participation customarily is restricted to executive officers with approval of the Compensation Committee. These benefit plans, reviewed periodically to ensure that they continue to meet their objectives, are as follows: (i) the Executive Survivor Benefits Plan, which provides a supplemental death benefit in addition to the voluntary life insurance plan provided to all employees; and (ii) the Executive Benefit Retirement Plan, a final average pay pension plan. These plans were frozen to new participants in 2010 and 2007, respectively.

The Compensation Committee discontinued the Company s Executive Medical Plan and Executive Salary Continuation Program, effective January 1, 2008, and in the place of the Executive Medical Plan, approved a policy allowing for the reimbursement of expenses associated with the annual physical examination of executive officers and their spouses.

The Company also offers two voluntary nonqualified deferred compensation plans: (i) the Deferred Compensation Administration Plan III (DCAP III); and (ii) the Supplemental Profit-Sharing Investment Plan II (SPSIP II). These plans are not tax-qualified plans under the U.S. Internal Revenue Code of 1986, as amended (the Code). The DCAP III is offered to all employees eligible for the MIP with a bonus target of at least 15% of base salary, including all executive officers and other selected highly compensated employees. The SPSIP II is offered to all employees, including executive officers, who may be impacted by the compensation limits that restrict participation in the Company s tax-qualified 401(k) plan, the Profit-Sharing Investment Plan (PSIP).

Guided by the Company s Executive Officer Security Policy for security, protection and privacy reasons, the Board has directed our CEO to use the corporate aircraft for both business and personal travel when practicable. By providing a confidential and controlled environment for conducting business without the scheduling constraints imposed by commercial airline service, the aircraft allows our employees, including the CEO, to be more productive than if commercial flights were utilized. For these same reasons, during FY 2012 our CEO authorized the use of corporate aircraft for personal use by Mr. Julian. Likewise, as directed by the Company s Executive Officer Security Policy, during FY 2012 the Company provided security services for Mr. Hammergren, including reimbursement of reasonable expenses related to installation and maintenance of home security. A car and driver are available for use by Mr. Hammergren, Mr. Julian and other executive officers.

Severance and Change in Control Benefits

Our Change in Control Policy for Selected Executive Employees (the CIC Policy) allows selected senior executives, including most of our NEOs, to receive certain double trigger benefits in the event of a qualifying termination of employment occurring in connection with a change in control. The CIC Policy is administered by the Compensation Committee and we believe its benefits are consistent with current market practice. The establishment of the CIC Policy recognizes that as with nearly every public company, the possibility of a change in control exists, and there is a need to reinforce and encourage in such circumstances the continued attention and dedication of senior management to maximizing stockholder value. The CIC Policy does not apply to Mr. Hammergren or Mr. Julian, as their severance pay is governed by their individual employment agreements. A detailed description of our CIC Policy and Messrs. Hammergren s and Julian s employment agreements is provided

below under the subsection entitled Executive Employment Agreements Change in Control Policy.

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Consistent with current market practice and the Company s CIC Policy, each of the Company s stockholder-approved equity compensation plans includes change in control provisions, providing for no change in the timing of vesting unless there is an involuntary or constructive termination of employment following a change in control.

Our Severance Policy for Executive Employees (Executive Severance Policy) affords benefits that are consistent with current market practice to selected management employees, including those executive officers who do not have employment agreements. The policy applies if an executive officer is terminated by the Company for reasons other than for Cause, as defined in the Executive Severance Policy, and the termination is not covered by the Company s CIC Policy. The Executive Severance Policy does not apply to Mr. Hammergren or Mr. Julian, as their severance pay is governed by their individual employment agreements. A detailed description of the Executive Severance Policy is provided below under the subsection entitled Executive Employment Agreements Executive Severance Policy.

Mr. Hammergren s employment agreement provides for severance benefits in the case of voluntary, involuntary and constructive termination with or without a change in control, as defined in his agreement and summarized below under Executive Employment Agreements. Mr. Hammergren s employment agreement, in substantially its current form, was extended to him when he was offered the position of co-chief executive officer in 1999.

The agreement s severance provisions, including provisions regarding pension rights, are not materially different from the agreement of his predecessor and have been in place for many years with one exception. On March 27, 2012, Mr. Hammergren delivered to Alton F. Irby III, Chair of the Compensation Committee, a letter relinquishing his right under his employment agreement to be paid a golden parachute tax gross-up, and the right to have his change in control-related cash severance calculated as the product of 2.99 times his base amount (as defined in Code Section 280G), leaving in place the alternative cash severance formulation of a lump sum equal to three years salary continuation and MIP participation. The relinquishment of these rights represents a substantial reduction in the potential benefits to which Mr. Hammergren would be entitled if he incurred a qualifying termination of employment in connection with a change in control of McKesson.

Information on Other Compensation-Related Topics

Executive Employment Agreements

We have generally discontinued the practice of providing our executive officers with an employment agreement. It is possible, however, that we may in the future enter into such an agreement if it is deemed in the best interests of our stockholders and necessary for the attraction and/or retention of a highly qualified candidate. We currently have employment agreements with Messrs. Hammergren and Julian, which were originally entered into in 1996 and 1999, respectively, coincident to their appointment to executive officer positions at McKesson. These are the only two employment agreements in place among our current roster of executive officers. Consistent with the Company s ICARE principles, we continue to honor our legacy contractual commitments.

Stock Ownership Policy

The Company has long-standing guidelines for stock ownership by executive officers (the Stock Ownership Policy), which was most recently modified in January 2010. Our CEO s holding requirement is expressed as ten times his base salary, and the holding requirement for each of the Company s other executive officers is expressed as six times his or her base salary. As shown in the table below, as of May 31, 2012 each of our NEOs has satisfied the Stock Ownership Policy. The Company reserves the right to restrict sales of the underlying shares of common stock delivered when equity awards vest, should the executive fail to meet his or her ownership requirement as specified in the Stock Ownership Policy.

The target ownership requirements, and the NEOs compliance with these requirements, are set forth in the table below.

Stock Ownership Policy

	Target Ownership Requirement		Actual Ownership	
Name	**Multiple of Base Salary**	**Multiple Expressed in Dollars**	**Multiple of Base Salary[(1)]**	**Value of Shares Held by Executive[(2)]**
John H. Hammergren	10	$16,800,000	72	$121,298,951
Jeffrey C. Campbell	6	$5,178,000	36	$30,913,005
Paul C. Julian	6	$6,390,000	36	$38,449,633

Marc E. Owen	6	$4,086,000	24	$16,511,456
Laureen E. Seeger	6	$4,116,000	22	$15,151,546

(1) NEO ownership is stated as of May 31, 2012. The ownership requirement may be met through any combination of the following:

Direct stock holdings of the Company s common stock, including shares held in a living trust or by a family partnership or corporation controlled by the officer, unless the officer expressly disclaims beneficial ownership of such shares;

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Shares of the Company s common stock held in the PSIP (*i.e.*, the Company s 401(k) plan);

Shares of the Company s common stock underlying outstanding restricted stock and restricted stock unit awards; and/or

Shares of the Company s common stock underlying restricted stock units that are vested and deferred under a Company-sponsored deferral program.

In all circumstances, stock options and performance restricted stock units (*i.e.*, PeRSUs) do not count towards meeting the required stock ownership.

(2) Based on the closing price of the Company s common stock as of May 31, 2012, which was $87.28 as reported by the NYSE.

The Company s directors are also subject to stock ownership guidelines, which are summarized above in the subsection entitled Director Stock Ownership Guidelines.

Insider Trading Policy and Hedging Prohibition

The Company maintains an insider trading policy applicable to all directors and employees. The policy provides that the Company s personnel may not buy, sell or engage in other transactions in the Company s stock while in possession of material non-public information; buy or sell securities of other companies while in possession of material non-public information about those companies that they become aware of as a result of business dealings between the Company and those companies; disclose material non-public information to any unauthorized persons outside of the Company; or engage in hedging transactions through the use of certain derivatives, such as put and call options involving the Company s securities, other than the exercise of any Company-issued stock option for cash. The policy also restricts trading for a limited group of Company employees (including all directors and NEOs) to defined window periods that follow our quarterly earnings releases.

Equity Grant Practices

The Company has adopted a written policy stating that stock options will be awarded at an exercise price equal to the closing price of the Company s common stock reported on the date of grant. In most situations, the date of grant is the same day that the Compensation Committee meets to approve the grant. From time-to-time, the Compensation Committee s meeting occurs shortly before or after the Company s earnings are released to the investment community. When this occurs, the Compensation Committee delays setting the equity grant date to the third trading day following the date the Company s earnings are released to the investment community. Under the terms of our 2005 Stock Plan, stock option re-pricing is not permitted without stockholder approval.

Stock option awards vest ratably over four years with a contractual term of seven years. PeRSU awards are a four year program, which following the initial one-year performance period, are converted into an RSU award that cliff-vests upon completion of the fourth year.

Tax Deductibility

Section 162(m) of the Internal Revenue Code generally provides that publicly held corporations may not deduct in any taxable year specified compensation in excess of $1,000,000 paid to the CEO and the next three most highly compensated executive officers, excluding the chief financial officer. However, performance-based compensation in excess of $1,000,000 is deductible if specified criteria are met, including stockholder approval of the materials terms of applicable plans. The Compensation Committee s intention is, and has always been, to comply with the requirements of Code Section 162(m) unless the Compensation Committee concludes that adherence to the limitations imposed by these provisions would not be in the best interest of the Company or its stockholders. While base salary in excess of $1,000,000 is not deductible, payments made under our MIP and LTIP programs, the grants of RSUs made under our PeRSU program, and the grants of stock option awards, are intended to qualify for deductibility under Code Section 162(m) as performance-based compensation.

For purposes of compliance with the Code, awards under these programs will not be made to individuals subject to Section 162(m), which includes our NEOs, unless attainment of performance goals is certified by the Compensation Committee. In the event of attainment of the minimum performance goals under these programs, the Compensation Committee will then exercise negative discretion to adjust awards downwards from a potential maximum amount in order to satisfy requirements under Code Section 162(m), while still providing for awards based on Company and individual performance in accordance with the MIP, LTIP and PeRSU program description provided above under the subheading Executive Officer Compensation Elements.

Compensation Recoupment Policy

The Board is dedicated to maintaining and enhancing a culture that is focused on integrity and accountability, and that discourages conduct detrimental to the Company s sustainable growth. To that end, on January 20, 2010 the Board approved an updated Compensation Recoupment Policy (the Recoupment Policy) that both expands on and clarifies the previous clawback policies embedded in the Company s various incentive plans and programs. The updated Recoupment Policy applies to any Company employee who receives a cash or equity incentive award after January 20, 2010.

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Under the Recoupment Policy, and consistent with the Company s core values, the Board determined that it may be appropriate to recover annual or long-term incentive compensation provided in certain situations. Specifically, the Company may recoup incentive compensation from any employee if: (i) he or she engages in intentional misconduct pertaining to any financial reporting requirement under the federal securities laws resulting in the Company being required to prepare and file an accounting restatement with the SEC as a result of such misconduct, other than a restatement due to changes in accounting policy; (ii) there is a material negative revision of a financial or operating measure on the basis of which incentive compensation was awarded or paid to the employee; or (iii) he or she engages in any fraud, theft, misappropriation, embezzlement or dishonesty to the material detriment of the Company s financial results as filed with the SEC. If triggered, then to the fullest extent permitted by law, the Company may require the employee to reimburse the Company for all or a portion of any incentive compensation received in cash within the last 12 months, and remit to the Company any profits realized from the sale of the Company s common stock within the last 12 months.

As described in the Company s standard incentive plan award documentation, the Compensation Committee may also seek to recoup any economic gain from any employee who engages in conduct that is not in good faith, and which disrupts, damages, impairs or interferes with the business, reputation or employees of the Company.

Excise Tax Gross-Up Policy

At its May 2012 meeting, responding to stockholder feedback, the Compensation Committee determined that our policy prohibiting new excise tax gross-up provisions, originally adopted in 2009, should be extended to apply to agreements other than employment agreements with our executive officers. As amended, the Company may not enter into any new agreement with an executive officer, or a material amendment of an existing executive officer agreement, which provides for payment or reimbursement by the Company of excise taxes that are payable by such executive officer under Code Section 4999 as a result of a change in control of the Company. The Compensation Committee also clarified that this policy would not adversely affect any Company plan, policy or arrangement applicable to management employees generally that provides for the payment or reimbursement of taxes.

Supplemental Death Benefits

In January 2010, the Board froze the Company s Executive Survivor Benefits Plan to the then-current roster of participants, which includes all of our current executive officers, and approved a new executive death benefits policy to the effect that the Company will not enter into a new plan, program or agreement (a Benefit Agreement) with any executive officer, as defined by the federal securities laws, or a material amendment of an existing Benefit Agreement with any executive officer, which provides for a death benefit that is not generally provided to all employees, including salary continuation upon the death of an executive officer, unless such Benefit Agreement or material amendment thereto is approved by the Company s stockholders pursuant to an advisory vote. This plan will continue to provide for its remaining participants a supplemental death benefit in addition to the voluntary and company-provided life insurance plan afforded to all employees. A detailed description of this plan is available below under the subheading, Potential Payments upon Termination or Change in Control.

Compensation Committee Report on Executive Compensation

We have reviewed and discussed the Compensation Discussion and Analysis contained in this proxy statement with management. Based on such review and discussion, we have recommended to the Board of Directors that the Compensation Discussion and Analysis be included in this proxy statement and in McKesson Corporation s Annual Report on Form 10-K for the fiscal year ended March 31, 2012.

Compensation Committee of the

Board of Directors

Alton F. Irby III, Chair
M. Christine Jacobs
David M. Lawrence, M.D.
Edward A. Mueller

Compensation Committee Interlocks and Insider Participation

The members of the Compensation Committee are Alton F. Irby III, M. Christine Jacobs, David M. Lawrence and Edward A. Mueller. No member of the Compensation Committee is, or was during FY 2012, an officer or employee of the Company or any of its subsidiaries or a

former officer of the Company or any of its subsidiaries. In addition, during FY 2012, none of our executive officers served as a member of the board of directors or the compensation committee of any other entity that has one or more executive officers serving on our Board of Directors or Compensation Committee.

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2012 Summary Compensation Table

The following table sets forth information regarding compensation and benefits earned by: (i) our Chairman of the Board, President and Chief Executive Officer; (ii) our Executive Vice President and Chief Financial Officer; and (iii) the three other most highly compensated executive officers as of March 31, 2012 (collectively, our NEOs):

rincipal Position	Fiscal Year	Salary ($)	Stock Awards ($)(1)	Option Awards ($)(1)	Non-Equity Incentive Plan Compensation ($)(2)	Change in Pension Value and Nonqualified Deferred Compensation Earnings ($)(3)(4)	All Other Compensation ($)(5)	
nmergren	2012	1,680,000	8,601,530	6,133,206	12,827,520	10,075,558	362,508	3
President and	2011	1,664,615	12,185,796	7,370,750	9,860,400	14,072,640	511,951	4
tive Officer	2010	1,580,000	11,049,424	7,647,826	12,828,150	20,671,741	566,388	5
ampbell	2012	861,039	3,173,380	2,261,747	3,453,179	1,506,558	127,322	1
ice President	2011	838,615	4,509,704	2,731,945	2,613,750	1,265,881	126,411	1
inancial Officer	2010	798,000	4,293,818	2,678,617	3,362,000	2,333,001	158,355	1
an	2012	1,062,692	4,760,070	3,402,809	6,322,734	3,048,268		

Award Types

Options

A stock option is the right to purchase shares of our common stock at a fixed exercise price for a fixed period. An option under the 2006 Plan may be an incentive stock option or a nonstatutory stock option. The exercise price of an option granted under the 2006 Plan must be at least equal to the fair market value of the Company's common stock on the date of grant. In addition, the exercise price for any incentive stock option granted to any employee owning more than ten percent of our common stock may not be less than 110 percent of the fair market value of the Company's common stock on the date of grant.

An option granted under the 2006 Plan cannot be exercised until it becomes vested. The administrator establishes the vesting schedule of each option at the time of grant and the option will expire at the time established by the administrator. After termination of the optionee's service, he or she may exercise his or her option for the period stated in the option agreement, to the extent the option is vested on the date of termination. If termination is due to death or disability, the option usually will remain exercisable for twelve months following such termination. In all other cases, the option generally will remain exercisable for three months. Nevertheless, an option may never be exercised later than the expiration of its term. The term of any stock option may not exceed ten years, except

that with respect to any participant who owns ten percent or more of the voting power of all classes of the Company's outstanding capital stock, the term for incentive stock options must not exceed five years.

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Stock Awards

Stock awards are awards or issuances of shares of our common stock that vest in accordance with terms and conditions established by the administrator. Stock awards include stock units, which are bookkeeping entries representing an amount equivalent to the fair market value of a share of common stock, payable in cash, property, or other shares of stock. The administrator may determine the number of shares to be granted, and impose whatever conditions to vesting it determines to be appropriate, including performance criteria and level of achievement versus the criteria that the administrator determines. The criteria may be based on financial performance, personal performance evaluations, and completion of service by the participant. Unless the administrator determines otherwise, shares that do not vest typically will be subject to forfeiture or to a right of repurchase of the unvested portion of such shares at the original price paid by the participant, which the Company may exercise upon the voluntary or involuntary termination of the awardee's service with the Company for any reason, including death or disability.

For stock awards intended to qualify as "performance-based compensation" within the meaning of Section 162(m) of the Code, the measures established by the administrator must be qualifying performance criteria, as defined by the 2006 Plan.

Stock Appreciation Rights

A stock appreciation right is the right to receive the appreciation in the fair market value of our common stock in an amount equal to the difference between (a) the fair market value of a share of our common stock on the date of exercise, and (b) the exercise price. This amount will be paid, as determined by the administrator, in shares of our common stock with equivalent value, cash, or a combination of both. The exercise price must be at least equal to the fair market value of our common stock on the date of grant. Subject to these limitations, the administrator determines the exercise price, term, vesting schedule, and other terms and conditions of stock appreciation rights, except that stock appreciation rights terminate under the same rules that apply to stock options.

Cash Awards

Cash awards confer upon the participant the opportunity to earn future cash payments tied to the level of achievement with respect to one or more performance criteria established by the administrator for a performance period. The administrator will establish the performance criteria and level of achievement versus these criteria, which will determine the target and the minimum and maximum amount payable under a cash award. The criteria may be based

on financial performance or personal performance evaluations, or both. For cash awards intended to qualify as "performance-based compensation" within the meaning of Section 162(m) of the Code, the measures established by the administrator must be based on one or more qualifying performance criteria, as defined in the 2006 Plan, and specified in writing.

Other Provisions of the 2006 Plan

Transferability of Awards

Unless the administrator determines otherwise, the 2006 Plan does not permit the transfer of awards other than by beneficiary designation, will, or by the laws of descent or distribution, and only the participant may exercise an award during his or her lifetime.

Preemptive Rights

The 2006 Plan provides that no shares will be issued in violation of any preemptive rights held by any stockholder of the Company.

Adjustments upon Merger or Change in Control

The 2006 Plan provides that in the event of a merger with or into another corporation in which the Company is not the surviving entity or the Company's "change in control," including the sale of all or substantially all of the Company 's assets, and various other events, the Company 's board or the Committee may, in its discretion, provide for the assumption or substitution of, or adjustment to, each outstanding award; accelerate the vesting of options and stock appreciation rights, and terminate any restrictions on stock awards or cash awards; provide for the cancellation of awards in exchange for a cash payment to the participant; or provide for the cancellation of awards that have not been exercised or redeemed as of the relevant event.

REPORT OF THE AUDIT COMMITTEE OF THE BOARD OF DIRECTORS

The audit committee of the board of directors is comprised entirely of independent directors who meet the independence requirements of The NASDAQ and the SEC. The audit committee operates pursuant to a charter that is available on our website at www.radnet.com under Investor Relations – Corporate Governance.

The audit committee oversees our financial reporting process on behalf of the board of directors. Management is responsible for the preparation, presentation and integrity of the financial statements, including establishing accounting and financial reporting principles and designing systems of internal control over financial reporting. Our independent registered public accounting firm, Ernst & Young LLP ("Ernst & Young"), is responsible for expressing an opinion as to the conformity of our consolidated financial statements with generally accepted accounting principles.

In performing its responsibilities, the audit committee has reviewed and discussed, with management and Ernst & Young, the audited consolidated financial statements in our annual report on Form 10-K for the year ended December 31, 2008. The audit committee has also discussed with Ernst & Young matters required to be discussed by Statement on Auditing Standards 61, as amended (AICPA, Professional Standards, Vol. 1, AU Section 380), as adopted by the Public Company Accounting Oversight Board in Rule 3200T.

The audit committee has received the written disclosures and the letter from Ernst & Young required by applicable requirements of the Public Company Accounting Oversight Board regarding Ernst & Young's communications with the audit committee concerning independence, and has discussed Ernst & Young's independence with Ernst & Young.

Based on the reviews and discussions referred to above, the audit committee recommended to the board of directors that the audited consolidated financial statements of RadNet, Inc. be included in the Company's annual report on Form 10-K for the year ended December 31, 2008.

Audit Committee:
Marvin S. Cadwell
Lawrence L. Levitt
David L. Swartz

This report is submitted by the Audit Committee.

CERTAIN RELATIONSHIPS AND RELATED PARTY TRANSACTIONS

Howard G. Berger, M.D. is our President and Chief Executive Officer, chair of our board of directors, and owns approximately 15% of our outstanding common stock. Dr. Berger also owns, indirectly, 99% of the equity interests in Beverly Radiology Medical Group ("BRMG"). BRMG provides all of the professional medical services at most of our California facilities under a management agreement and contracts with various other independent physicians and physician groups to provide all of the professional medical services at most of our other California facilities. We obtain professional medical services from BRMG in California, rather than providing such services directly or through subsidiaries, in order to comply with California's prohibition against the corporate practice of medicine. However, as a result of this close relationship with Dr. Berger and BRMG, we believe that we are able to better ensure that professional medical services are provided at our California facilities in a manner consistent with our needs and expectations and those of our referring physicians, patients and payors than if we obtained these services from unaffiliated practice groups.

Under our management agreement with BRMG, which expires on January 1, 2014, BRMG pays us, as compensation for the use of our facilities and equipment and for our services, a percentage of the gross amounts collected for the professional services it renders. The percentage, which was 79%, at December 31, 2008, is adjusted annually, if necessary, to ensure that the parties receive fair value for the services they render. In operation and historically, the annual revenue of BRMG from all sources closely approximates its expenses, including Dr. Berger's compensation, fees payable to us and amounts payable to third parties. For administrative convenience and in order to avoid inconveniencing and confusing our payors, a single bill is prepared for both the professional medical services provided by the radiologists and our non-medical, or technical, services, generating a receivable for BRMG. BRMG maintains a $55 million revolving credit facility with General Electric Capital Corporation from which we may obtain funds by utilizing our accounts receivable for working capital purposes, if needed. We repay or offset these advances with periodic payments from BRMG to us under the management agreement. We guarantee BRMG's obligations under this working capital facility.

Dr. Crues and Dr. Berger receive all or a portion of their salary from BRMG (Please See Summary Compensation Table).

In April 2006, in order to induce Mr. Linden to continue his employment we issued to him a six year

warrant to purchase 250,000 shares of common stock at a price per share of $2.52, the public market price of our common stock on the date of issuance, vesting over a six year period.

Cohen & Lord, a professional corporation, a law firm with which Mr. Linden is associated, received $411,859 in fees during the year ended December 31, 2007 and $398,128 during the year ended December 31, 2008. Mr. Linden has specifically waived any interest in our fees since becoming an officer of the Company.

In March 2006 we extended the warrant originally issued to Norman R. Hames in connection with the acquisition of DIS by reissuing to Mr. Hames a seven year warrant to purchase 1,500,000 shares at an exercise price of $1.12 per share, the public market price of our common stock on the date of the reissuance, vesting over the seven year period. We have agreed to provide to Mr. Hames a bonus of $.040 per share for each share exercised. In January 2008, Mr. Hames exercised certain warrants and received a bonus of $129,000.

In recognition of our chief financial officer, Mark D. Stolper's services to the Company, on July 11, 2006, the Company issued to Mr. Stolper a five-year warrant to purchase 100,000 shares of our common stock at $3.10 per share, the public market price of our common stock on the date of issuance.

On October 28, 2008, we issued five year options vesting over three years to purchase 150,000 shares each to our Executive Vice Presidents, Norman Hames, Steve Forthuber, Mark Stolper and Jeffrey Linden, at an exercise price of $3.24 per share, the public market price of our stock on the date of issuance.

As a matter of policy, the board reviews any transaction in which we are proposed to be a party, directly or indirectly, and any of the following persons or entities is or is entitled to be a party, directly or indirectly, to the transaction or any director has a material financial interest in the transaction: (i) any of our executive officers or any related person of any such officer or a director, (ii) any person or entity of which the executive officer or director or any related person is the owner of more than 5% of the securities, (iii) any person or entity that controls one or more of the persons specified in subparagraph (ii) or a person that is controlled by, or is under common control with one or more of the persons specified in subparagraph (ii), or (iv) an individual who is a general partner, principal or employer of a director. Additionally, any transaction which would be required to be disclosed pursuant to Item 404 by Regulation S-K of the Regulations of the SEC is reviewed by the board.

Indemnification Agreements

We have indemnification agreements with each of our directors and certain officers in addition to provisions which are reflected in our certificate of incorporation and bylaws which require us to indemnify our directors and officers to the fullest extent permitted by Delaware law.

OTHER MATTERS

We know of no other matters to be submitted at the annual meeting. If any other matters are properly brought before the annual meeting, it is the intention of the persons named in the enclosed proxy card to vote the shares that they represent in accordance with their judgment.

For further information about RadNet, Inc., please refer to our annual report on Form 10-K for the fiscal year ended December 31, 2008 which accompanies this proxy statement. Our annual report on Form 10-K was filed with the SEC on March 16, 2009, and is publicly available on our website at www.radnet.com. You may also obtain a copy by sending a written request to Investor Relations, RadNet, Inc., 1510 Cotner Ave., Los Angeles, CA 90025.

By order of the board of directors,

Norman R. Hames
Corporate Secretary

EXHIBIT A

RADNET, INC.
2006 EQUITY INCENTIVE PLAN

1. Purpose of the Plan. The purpose of this Plan is to encourage ownership in the Company by key personnel whose long-term service the Company considers essential to its continued progress and, thereby, encourage recipients to act in the stockholders' interest and share in the Company's success.

2. Definitions. As used herein, the following definitions shall apply:

"Act" shall mean the Securities Act of 1933, as amended.

"Administrator" shall mean the Board, any Committees, or such delegates as shall be administering the Plan in accordance with Section 4 of the Plan.

"Affiliate" shall mean any entity that is directly or indirectly in control of or controlled by the Company, or any entity in which the Company has a significant ownership interest as determined by the Administrator.

"Applicable Laws" shall mean the requirements relating to the administration of stock plans under federal and state laws; any stock exchange or quotation system on which the Company has listed or submitted for quotation the Common Stock to the extent provided under the terms of the Company's agreement with such exchange or quotation system; and, with respect to Awards subject to the laws of any foreign jurisdiction where Awards are, or will be, granted under the Plan, to the laws of such jurisdiction.

"Award" shall mean, individually or collectively, a grant under the Plan of an Option, Stock Award, SAR, or Cash Award.

"Awardee" shall mean a Service Provider who has been granted an Award under the Plan.

"Award Agreement" shall mean an Option Agreement, Stock Award Agreement, SAR Agreement, or Cash Award Agreement, which may be in written or electronic format, in such form and with such terms as may be specified by the Administrator, evidencing the terms and conditions of an individual Award. Each Award Agreement is subject to the terms and conditions of the Plan.

"Board" shall mean the Board of Directors of the Company.

"Cash Award" shall mean a bonus opportunity awarded under Section 13 pursuant to which a Participant may become entitled to receive an amount based on the satisfaction of such performance criteria as are specified in the agreement or other documents evidencing the Award (the "Cash Award Agreement").

"Change in Control" shall mean any of the following, unless the Administrator provides otherwise:

(i) any merger or consolidation in which the Company shall not be the surviving entity (or survives only as a subsidiary of another entity whose stockholders did not own all or substantially all of the Common Stock in substantially the same proportions as immediately before such transaction);

(ii) the sale of all or substantially all of the Company's assets to any other person or entity (other than a wholly-owned subsidiary of the Company);

(iii) the acquisition of beneficial ownership of a controlling interest (including power to vote) in the outstanding shares of Common Stock by any person or entity (including a "group" as defined by or under Section 13(d)(3) of the Exchange Act);

(iv) the dissolution or liquidation of the Company;

(v) a contested election of Directors, as a result of which or in connection with which the persons who were Directors before such election or their nominees cease to constitute a majority of the Board; or

(vi) any other event specified, at the time an Award is granted or thereafter, by the Board or a Committee.

Notwithstanding the foregoing, the term "Change in Control" shall not include any underwritten public offering of Shares registered under the Act.

"Code" shall mean the Internal Revenue Code of 1986, as amended.

"Committee" shall mean a committee of Directors appointed by the Board in accordance with Section 4 of the Plan.

"Common Stock" shall mean the common stock of the Company, par value $0.01.

"Company" shall mean RadNet, Inc., a Delaware corporation, or its successor.

"Consultant" shall mean any natural person, other than an Employee or Director, who performs bona fide services for the Company or an Affiliate as a consultant or advisor.

"Conversion Award" has the meaning set forth in Section 4(b)(xii) of the Plan.

"Director" shall mean a member of the Board.

"Disability" shall mean permanent and total disability as defined in Section 22(e)(3) of the Code.

"Employee" shall mean an employee of the Company or any Affiliate, and may include an Officer or Director. Within the limitations of Applicable Law, the Administrator shall have the discretion to determine the effect upon an Award and upon an individual's status as an Employee in the case of (i) any individual who is classified by the Company or its Affiliate as leased from or otherwise employed by a third party or as intermittent or temporary, even if any such classification is changed retroactively as a result of an audit, litigation or otherwise; (ii) any leave of absence approved by the Company or an Affiliate; (iii) any transfer between locations of employment with the Company or an Affiliate or between the Company and any Affiliate or between any Affiliates; (iv) any change in the Awardee's status from an employee to a Consultant or Director; and (v) an employee who, at the request of the Company or an Affiliate, becomes employed by any partnership, joint venture, or corporation not meeting the requirements of an Affiliate in which the Company or an Affiliate is a party.

"Exchange Act" shall mean the Securities Exchange Act of 1934, as amended.

"Fair Market Value" shall mean, unless the Administrator determines otherwise, as of any date, the closing price for such Common Stock as of such date (or if no sales were reported on such date, the closing price on the last preceding day for which a sale was reported), as reported in such source as the Administrator shall determine.

"Grant Date" shall mean the date upon which an Award is granted to an Awardee pursuant to this Plan.

"Incentive Stock Option" shall mean an Option intended to qualify as an incentive stock option within the meaning of Section 422 of the Code.

"Nonstatutory Stock Option" shall mean an Option not intended to qualify as an Incentive Stock Option.

"Officer" shall mean a person who is an officer of the Company within the meaning of Section 16 of the Exchange Act.

"Option" shall mean a right granted under Section 8 of the Plan to purchase a certain number of Shares at such exercise price, at such times, and on such other terms and conditions as are specified in the agreement or other documents evidencing the Award (the "Option Agreement"). Both Options intended to qualify as Incentive Stock Options and Nonstatutory Stock Options may be granted under the Plan.

"Participant" shall mean the Awardee or any person (including any estate) to whom an Award has been

assigned or transferred as permitted hereunder.

"Plan" shall mean this RadNet, Inc. 2006 Equity Incentive Plan.

"Qualifying Performance Criteria" shall have the meaning set forth in Section 14(b) of the Plan.

"Related Corporation" shall mean any parent or subsidiary (as those terms are defined in Section 424(e) and (f) of the Code) of the Company.

"Service Provider" shall mean an Employee, Officer, Director, or Consultant.

"Share" shall mean a share of the Common Stock, as adjusted in accordance with Section 15 of the Plan.

"Stock Award" shall mean an award or issuance of Shares or Stock Units made under Section 11 of the Plan, the grant, issuance, retention, vesting, and transferability of which is subject during specified periods to such conditions (including continued service or performance conditions) and terms as are expressed in the agreement or other documents evidencing the Award (the "Stock Award Agreement").

"Stock Appreciation Right" or "SAR" shall mean an Award, granted alone or in connection with an Option, that pursuant to Section 12 of the Plan is designated as a SAR. The terms of the SAR are expressed in the agreement or other documents evidencing the Award (the "SAR Agreement").

"Stock Unit" shall mean a bookkeeping entry representing an amount equivalent to the fair market value of one Share, payable in cash, property or Shares. Stock Units represent an unfunded and unsecured obligation of the Company, except as otherwise provided for by the Administrator.

"Ten-Percent Stockholder" shall mean the owner of stock (as determined under Section 424(d) of the Code) possessing more than 10% of the total combined voting power of all classes of stock of the Company (or any Related Corporation).

"Termination Date" shall mean the date of a Participant's Termination of Service, as determined by the Administrator in its sole discretion.

"Termination of Service" shall mean ceasing to be a Service Provider. However, for Incentive Stock Option purposes, Termination of Service will occur when the Awardee ceases to be an employee (as determined in accordance with Section 3401(c) of the Code and the regulations promulgated thereunder) of the Company or one of its Related Corporations. The Administrator shall determine whether any corporate transaction, such as a sale or spin-off of a division or business unit, or a joint venture, shall be deemed to result in a Termination of Service.

3. Stock Subject to the Plan.

(a) Aggregate Limits.

(i) The maximum aggregate number of Shares that may be issued under the Plan through Awards is 6,500,000 Shares. Notwithstanding the foregoing, the maximum aggregate number of Shares that may be issued under

the Plan through Incentive Stock Options is 6,500,000 Shares. The limitations of this Section 3(a)(i) shall be subject to the adjustments provided for in Section 15 of the Plan.

(ii) Upon payment in Shares pursuant to the exercise of an Award, the number of Shares available for issuance under the Plan shall be reduced only by the number of Shares actually issued in such payment. If any outstanding Award expires or is terminated or canceled without having been exercised or settled in full, or if Shares acquired pursuant to an Award subject to forfeiture or repurchase are forfeited or repurchased by the Company, the Shares allocable to the terminated portion of such Award or such forfeited or repurchased Shares shall again be available to grant under the Plan. Notwithstanding the foregoing, the aggregate number of shares of Common Stock that may be issued under the Plan upon the exercise of Incentive Stock Options shall not be increased for restricted Shares that are forfeited or repurchased. Notwithstanding anything in the Plan, or any Award Agreement to the contrary, Shares attributable to Awards transferred under any Award transfer program shall not be again available for grant under the Plan. The Shares subject to the Plan may be either Shares reacquired by the Company, including Shares purchased in the open market, or authorized but unissued Shares.

(b) Code Section 162(m) Limit. Subject to the provisions of Section 15 of the Plan, the aggregate number of Shares subject to Awards granted under this Plan during any calendar year to any one Awardee shall not exceed 125,000 except that in connection with his or her initial service, an Awardee may be granted Awards covering up to an additional 125,000 Shares. Notwithstanding anything to the contrary in the Plan, the limitations set forth in this Section 3(b) shall be subject to adjustment under Section 15 of the Plan only to the extent that such adjustment will not affect the status of any Award intended to qualify as "performance-based compensation" under Code Section 162(m).

4. Administration of the Plan.

(a) Procedure.

(i) Multiple Administrative Bodies. The Plan shall be administered by the Board or one or more Committees, including such delegates as may be appointed under paragraph (a)(iv) of this Section 4.

(ii) Section 162(m). To the extent that the Administrator determines it to be desirable to qualify Awards granted hereunder as "performance-based compensation" within the meaning of Section 162(m) of the Code, Awards to "covered employees" within the meaning of Section 162(m) of the Code or Employees that the Committee determines may be "covered employees" in the future shall be made by a Committee of two or more "outside directors" within the meaning of Section 162(m) of the Code.

(iii) Rule 16b-3. To the extent desirable to qualify transactions hereunder as exempt under Rule 16b-3 promulgated under the Exchange Act ("Rule 16b-3"), Awards to Officers and Directors shall be made in such a manner to satisfy the requirement for exemption under Rule 16b-3.

(iv) Other Administration. The Board or a Committee may delegate to an authorized Officer or Officers of the Company the power to approve Awards to persons eligible to receive Awards under the Plan who are not (A) subject to Section 16 of the Exchange Act; or (B) at the time of such approval, "covered employees" under Section 162(m) of the Code.

(v) Delegation of Authority for the Day-to-Day Administration of the Plan. Except to the extent prohibited by Applicable Law, the Administrator may delegate to one or more individuals the day-to-day administration of the Plan and any of the functions assigned to it in this Plan. Such delegation may be revoked at any time.

(b) Powers of the Administrator. Subject to the provisions of the Plan and, in the case of a Committee or delegates acting as the Administrator, subject to the specific duties delegated to such Committee or delegates, the Administrator shall have the authority, in its sole discretion:

(i) to select the Service Providers of the Company or its Affiliates to whom Awards are to be granted hereunder;

(ii) to determine the number of shares of Common Stock to be covered by each Award granted hereunder;

(iii) to determine the type of Award to be granted to the selected Service Provider;

(iv) to approve the forms of Award Agreements for use under the Plan;

(v) to determine the terms and conditions, consistent with the terms of the Plan, of any Award granted hereunder. Such terms and conditions include the exercise or purchase price, the time or times when an Award may be exercised (which may or may not be based on performance criteria), the vesting schedule, any vesting or exercisability acceleration or waiver of forfeiture restrictions, the acceptable forms of consideration, the term, and any restriction or limitation regarding any Award or the Shares relating thereto, based in each case on such factors as the Administrator, in its sole discretion, shall determine and may be established at the time an Award is granted or thereafter;

(vi) to correct administrative errors;

(vii) to construe and interpret the terms of the Plan (including sub-plans and Plan addenda) and Awards granted pursuant to the Plan;

(viii) to adopt rules and procedures relating to the operation and administration of the Plan to accommodate the specific requirements of local laws and procedures. Without limiting the generality of the foregoing, the Administrator is specifically authorized (A) to adopt the rules and procedures regarding the conversion of local currency, withholding procedures, and handling of stock certificates that vary with local requirements; and (B) to adopt sub-plans and Plan addenda as the Administrator deems desirable, to accommodate foreign laws, regulations and practice;

(ix) to prescribe, amend and rescind rules and regulations relating to the Plan, including rules and regulations relating to sub-plans and Plan addenda;

(x) to modify or amend each Award, including the acceleration of vesting, exercisability, or both; provided, however, that any modification or amendment of an Award is subject to Section 16 of the Plan and may not materially impair any outstanding Award unless agreed to by the Participant;

(xi) to allow Participants to satisfy withholding tax amounts by electing to have the Company withhold from the Shares to be issued pursuant to an Award that number of Shares having a Fair Market Value equal to the amount required to be withheld. The Fair Market Value of the Shares to be withheld shall be determined in such manner and on such date that the Administrator shall determine or, in the absence of provision otherwise, on the date that the amount of tax to be withheld is to be determined. All elections by a Participant to have Shares withheld for this purpose shall be made in such form and under such conditions as the Administrator may provide;

(xii) to authorize conversion or substitution under the Plan of any or all stock options, stock appreciation rights, or other stock awards held by service providers of an entity acquired by the Company (the "Conversion Awards"). Any conversion or substitution shall be effective as of the close of the merger or acquisition. The Conversion Awards may be Nonstatutory Stock Options or Incentive Stock Options, as determined by the Administrator, with respect to options granted by the acquired entity. Unless otherwise determined by the Administrator at the time of conversion or substitution, all Conversion Awards shall have the same terms and conditions as Awards generally granted by the Company under the Plan;

(xiii) to authorize any person to execute on behalf of the Company any instrument required to effect the grant of an Award previously granted by the Administrator;

(xiv) to determine whether Awards will be settled in Shares, cash, or in any combination thereof;

(xv) to determine whether to provide for the right to receive dividends or dividend equivalents;

(xvi) to establish a program whereby Service Providers designated by the Administrator can reduce compensation otherwise payable in cash in exchange for Awards under the Plan;

(xvii) to impose such restrictions, conditions, or limitations as it determines appropriate as to the timing

and manner of any resales by a Participant or other subsequent transfers by the Participant of any Shares issued as a result of or under an Award, including (A) restrictions under an insider trading policy, and (B) restrictions as to the use of a specified brokerage firm for such resales or other transfers;

(xviii) to provide, either at the time an Award is granted or by subsequent action, that an Award shall contain as a term thereof, a right, either in tandem with the other rights under the Award or as an alternative thereto, of the Participant to receive, without payment to the Company, a number of Shares, cash, or a combination of both, the amount of which is determined by reference to the value of the Award; and

(xix) to make all other determinations deemed necessary or advisable for administering the Plan and any Award granted hereunder.

(c) Effect of Administrator's Decision. All decisions, determinations and interpretations by the Administrator regarding the Plan, any rules and regulations under the Plan and the terms and conditions of any Award granted hereunder, shall be final and binding on all Participants. The Administrator shall consider such factors as it deems relevant, in its sole and absolute discretion, to making such decisions, determinations and interpretations, including the recommendations or advice of any officer or other employee of the Company and such attorneys, consultants and accountants as it may select.

5. Eligibility. Awards may be granted to Service Providers of the Company or any of its Affiliates.

6. Effective Date and Term of the Plan. Subject to stockholder approval, the Plan shall become effective upon its adoption by the Board. Options, SARs, and Cash Awards may be granted immediately thereafter; provided, that no Option or SAR may be exercised and no Stock Award may be granted under the Plan until it is approved by the stockholders of the Company, in the manner and to the extent required by Applicable Law, within 12 months after the date of adoption by the Board. The Plan shall continue in effect for a term of ten years from the date of the Plan's adoption by the Board unless terminated earlier under Section 16 herein.

7. Term of Award. The term of each Award shall be determined by the Administrator and stated in the Award Agreement. In the case of an Option, the term shall be ten years from the Grant Date or such shorter term as may be provided in the Award Agreement.

8. Options. The Administrator may grant an Option or provide for the grant of an Option, from time to time in the discretion of the Administrator or automatically upon the occurrence of specified events, including the achievement of performance goals, and for the satisfaction of an event or condition within the control of the Awardee or within the control of others.

(a) Option Agreement. Each Option Agreement shall contain provisions regarding (i) the number of Shares

that may be issued upon exercise of the Option; (ii) the type of Option; (iii) the exercise price of the Shares and the means of payment for the Shares; (iv) the term of the Option; (v) such terms and conditions on the vesting or exercisability of an Option, or both, as may be determined from time to time by the Administrator; (vi) restrictions on the transfer of the Option and forfeiture provisions; and (vii) such further terms and conditions, in each case not inconsistent with this Plan, as may be determined from time to time by the Administrator.

(b) Exercise Price. The per share exercise price for the Shares to be issued pursuant to exercise of an Option shall be determined by the Administrator, subject to the following:

(i) In the case of an Incentive Stock Option, the per Share exercise price shall be no less than 100% of the Fair Market Value per Share on the Grant Date. Notwithstanding the foregoing, if any Incentive Stock Option is granted to a Ten-Percent Stockholder, then the exercise price shall not be less than 110% of the Fair Market Value of a share of Common Stock on the Grant Date.

(ii) In the case of a Nonstatutory Stock Option, the per Share exercise price shall be no less than 100% of the Fair Market Value per Share on the Grant Date. The per Share exercise price may also vary according to a predetermined formula; provided, that the exercise price never falls below 100% of the Fair Market Value per Share on the Grant Date.

(iii) Notwithstanding the foregoing, at the Administrator's discretion, Conversion Awards may be granted in substitution or conversion of options of an acquired entity, with a per Share exercise price of less than 100% of the Fair Market Value per Share on the date of such substitution or conversion.

(c) Vesting Period and Exercise Dates. Options granted under this Plan shall vest, be exercisable, or both, at such times and in such installments during the Option's term as determined by the Administrator. The Administrator shall have the right to make the timing of the ability to exercise any Option granted under this Plan subject to continued service, the passage of time, or such performance requirements as deemed appropriate by the Administrator. At any time after the grant of an Option, the Administrator may reduce or eliminate any restrictions surrounding any Participant's right to exercise all or part of the Option.

(d) Form of Consideration. The Administrator shall determine the acceptable form of consideration for exercising an Option, including the method of payment, either through the terms of the Option Agreement or at the time of exercise of an Option. The consideration, determined by the Administrator (or pursuant to authority expressly delegated by the Board, a Committee, or other person), and in the form and amount required by applicable law, shall be actually received before issuing any Shares pursuant to the Plan; which consideration shall have a value, as determined by the Board, not less than the par value of such Shares. Acceptable forms of consideration may include:

(i) cash;

(ii) check or wire transfer;

(iii) subject to any conditions or limitations established by the Administrator, other Shares that have a Fair Market Value on the date of surrender or attestation that does not exceed the aggregate exercise price of the Shares as to which said Option shall be exercised;

(iv) consideration received by the Company under a broker-assisted sale and remittance program acceptable to the Administrator to the extent that this procedure would not violate Section 402 of the Sarbanes-Oxley Act of 2002, as amended;

(v) cashless, subject to any conditions or limitations established by the Administrator;

(vi) such other consideration and method of payment for the issuance of Shares to the extent permitted by Applicable Laws; or

(vii) any combination of the foregoing methods of payment.

9. Incentive Stock Option Limitations.

(a) Eligibility. Only employees (as determined in accordance with Section 3401(c) of the Code and the regulations promulgated thereunder) of the Company or any of its Related Corporations may be granted Incentive Stock Options.

(b) $100,000 Limitation. Notwithstanding the designation "Incentive Stock Option" in an Option Agreement, if the aggregate Fair Market Value of the Shares with respect to which Incentive Stock Options are exercisable for the first time by the Awardee during any calendar year (under all plans of the Company and any of its Related Corporations) exceeds $100,000, then the portion of such Options that exceeds $100,000 shall be treated as Nonstatutory Stock Options. An Incentive Stock Option is considered to be first exercisable during a calendar year if the Incentive Stock Option will become exercisable at any time during the year, assuming that any condition on the Awardee's ability to exercise the Incentive Stock Option related to the performance of services is satisfied. If the Awardee's ability to exercise the Incentive Stock Option in the year is subject to an acceleration provision, then the Incentive Stock Option is considered first exercisable in the calendar year in which the acceleration provision is triggered. For purposes of this Section 9(b), Incentive Stock Options shall be taken into account in the order in which they were granted. However, because an acceleration provision is not taken into account before its triggering, an Incentive Stock Option that becomes exercisable for the first time during a calendar year by operation of such provision does not affect the application of the $100,000 limitation with respect to any Incentive Stock Option (or portion thereof) exercised before such acceleration. The Fair Market Value of the Shares shall be determined as of the Grant Date.

(c) Leave of Absence. For purposes of Incentive Stock Options, no leave of absence may exceed three months, unless the right to reemployment upon expiration of such leave is provided by statute or contract. If the period of leave exceeds three months and the Awardee's right to reemployment is not provided by statute or contract, the Awardee's employment with the Company shall be deemed to terminate on the first day immediately following such three-month period, and any Incentive Stock Option granted to the Awardee shall cease to be treated as an Incentive Stock Option and shall terminate upon the expiration of the three-month period starting on the date the employment relationship is deemed terminated.

(d) Transferability. The Option Agreement must provide that an Incentive Stock Option cannot be transferable by the Awardee otherwise than by will or the laws of descent and distribution, and, during the lifetime of such Awardee, must not be exercisable by any other person. Notwithstanding the foregoing, the Administrator, in its sole discretion, may allow the Awardee to transfer his or her Incentive Stock Option to a trust where under Section 671 of the Code and other Applicable Law, the Awardee is considered the sole beneficial owner of the Option while it is held in the trust. If the terms of an Incentive Stock Option are amended to permit transferability, the Option will be treated for tax purposes as a Nonstatutory Stock Option.

(e) Exercise Price. The per Share exercise price of an Incentive Stock Option shall be determined by the Administrator in accordance with Section 8(b)(i) of the Plan.

(f) Ten-Percent Stockholder. If any Incentive Stock Option is granted to a Ten-Percent Stockholder, then the Option term shall not exceed five years measured from the date of grant of such Option.

(g) Other Terms. Option Agreements evidencing Incentive Stock Options shall contain such other terms and conditions as may be necessary to qualify as Incentive Stock Options, to the extent determined desirable by the Administrator, under the applicable provisions of Section 422 of the Code.

10. Exercise of Option.

(a) Procedure for Exercise; Rights as a Stockholder.

(i) Any Option granted hereunder shall be exercisable according to the terms of the Plan and at such times and under such conditions as determined by the Administrator and set forth in the respective Award Agreement.

(ii) An Option shall be deemed exercised when the Company receives (A) written or electronic notice of exercise (in accordance with the Award Agreement) from the person entitled to exercise the Option; (B) full payment for the Shares with respect to which the related Option is exercised; and (C) with respect to Nonstatutory Stock Options, payment of all applicable withholding taxes.

(iii) Shares issued upon exercise of an Option shall be issued in the name of the Participant or, if requested by the Participant, in the name of the Participant and his or her spouse. Unless provided otherwise by the Administrator or pursuant to this Plan, until the Shares are issued (as evidenced by the appropriate entry on the

books of the Company or of a duly authorized transfer agent of the Company), no right to vote or receive dividends or any other rights as a stockholder shall exist with respect to the Shares subject to an Option, notwithstanding the exercise of the Option.

(iv) The Company shall issue (or cause to be issued) such Shares as soon as administratively practicable after the Option is exercised. An Option may not be exercised for a fraction of a Share.

(b) Effect of Termination of Service on Options.

(i) Generally. Unless otherwise provided for by the Administrator, if a Participant ceases to be a Service Provider, other than upon the Participant's death or Disability, the Participant may exercise his or her Option within such period as is specified in the Award Agreement to the extent that the Option is vested on the Termination Date (but in no event later than the expiration of the term of such Option as set forth in the Award Agreement). In the absence of a specified time in the Award Agreement, the vested portion of the Option will remain exercisable for three months following the Participant's Termination Date. Unless otherwise provided by the Administrator, if on the Termination Date the Participant is not vested as to his or her entire Option, the Shares covered by the unvested portion of the Option will automatically revert to the Plan. If after the Termination of Service the Participant does not exercise his or her Option within the time specified by the Administrator, the Option will automatically terminate, and the Shares covered by such Option will revert to the Plan.

(ii) Disability of Awardee. Unless otherwise provided for by the Administrator, if a Participant ceases to be a Service Provider as a result of the Participant's Disability, the Participant may exercise his or her Option within such period as is specified in the Award Agreement to the extent the Option is vested on the Termination Date (but in no event later than the expiration of the term of such Option as set forth in the Award Agreement). In the absence of a specified time in the Award Agreement, the Option will remain exercisable for twelve months following the Participant's Termination Date. Unless otherwise provided by the Administrator, if at the time of Disability the Participant is not vested as to his or her entire Option, the Shares covered by the unvested portion of the Option will automatically revert to the Plan. If the Option is not so exercised within the time specified herein, the Option will terminate, and the Shares covered by such Option will automatically revert to the Plan.

(iii) Death of Awardee. Unless otherwise provided for by the Administrator, if a Participant dies while a Service Provider, the Option may be exercised following the Participant's death within such period as is specified in the Award Agreement to the extent that the Option is vested on the date of death (but in no event may the Option be exercised later than the expiration of the term of such Option as set forth in the Award Agreement), by the Participant's designated beneficiary, provided such beneficiary has been designated before the Participant's death in a form acceptable to the Administrator. If no such beneficiary has been designated by the Participant, then such Option may be exercised by the personal representative

of the Participant's estate or by the person or persons to whom the Option is transferred pursuant to the Participant's will or in accordance with the laws of descent and distribution. In the absence of a specified time in the Award Agreement, the Option will remain exercisable for twelve months following Participant's death. Unless otherwise provided by the Administrator, if at the time of death Participant is not vested as to his or her entire Option, the Shares covered by the unvested portion of the Option will revert to the Plan. If the Option is not so exercised within the time specified herein, the Option will terminate, and the Shares covered by such Option will revert to the Plan.

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11. Stock Awards.

(a) Stock Award Agreement. Each Stock Award Agreement shall contain provisions regarding (i) the number of Shares subject to such Stock Award or a formula for determining such number; (ii) the purchase price, if any, of the Shares, and the means of payment for the Shares; (iii) the performance criteria, if any, and level of achievement versus these criteria that shall determine the number of Shares granted, issued, retained, or vested, as applicable; (iv) such terms and conditions on the grant, issuance, vesting, or forfeiture of the Shares, as applicable, as may be determined from time to time by the Administrator; (v) restrictions on the transferability of the Stock Award; and (vi) such further terms and conditions in each case not inconsistent with this Plan as may be determined from time to time by the Administrator.

(b) Restrictions and Performance Criteria. The grant, issuance, retention, and vesting of each Stock Award may be subject to such performance criteria and level of achievement versus these criteria as the Administrator shall determine, which criteria may be based on financial performance, personal performance evaluations, or completion of service by the Awardee.

Notwithstanding anything to the contrary herein, the performance criteria for any Stock Award that is intended to satisfy the requirements for "performance-based compensation" under Section 162(m) of the Code shall be established by the Administrator based on one or more Qualifying Performance Criteria selected by the Administrator and specified in writing.

(c) Forfeiture. Unless otherwise provided for by the Administrator, upon the Awardee's Termination of Service, the unvested Stock Award and the Shares subject thereto shall be forfeited, provided that to the extent that the Participant purchased any Shares pursuant to such Stock Award, the Company shall have a right to repurchase the unvested portion of such Shares at the original price paid by the Participant.

(d) Rights as a Stockholder. Unless otherwise provided by the Administrator, the Participant shall have the rights equivalent to those of a stockholder and shall be a stockholder only after Shares are issued (as evidenced by the appropriate entry on the books of the Company or of a duly authorized transfer agent of the Company) to the Participant. Unless otherwise provided by the Administrator, a Participant holding Stock Units shall be entitled to receive dividend payments as if he or she were an actual stockholder.

12. Stock Appreciation Rights. Subject to the terms and conditions of the Plan, a SAR may be granted to a

Service Provider at any time and from time to time as determined by the Administrator in its sole discretion.

(a) Number of SARs. The Administrator shall have complete discretion to determine the number of SARs granted to any Service Provider.

(b) Exercise Price and Other Terms. The per SAR exercise price shall be no less than 100% of the Fair Market Value per Share on the Grant Date. The Administrator, subject to the provisions of the Plan, shall have complete discretion to determine the other terms and conditions of SARs granted under the Plan.

(c) Exercise of SARs. SARs shall be exercisable on such terms and conditions as the Administrator, in its sole discretion, shall determine.

(d) SAR Agreement. Each SAR grant shall be evidenced by a SAR Agreement that will specify the exercise price, the term of the SAR, the conditions of exercise, and such other terms and conditions as the Administrator, in its sole discretion, shall determine.

(e) Expiration of SARs. A SAR granted under the Plan shall expire upon the date determined by the Administrator, in its sole discretion, and set forth in the SAR Agreement. Notwithstanding the foregoing, the rules of Section 10(b) will also apply to SARs.

(f) Payment of SAR Amount. Upon exercise of a SAR, the Participant shall be entitled to receive a payment from the Company in an amount equal to the difference between the Fair Market Value of a Share on the date of exercise over the exercise price of the SAR. This amount shall be paid in cash, Shares of equivalent value, or a combination of both, as the Administrator shall determine.

13. Cash Awards. Each Cash Award will confer upon the Participant the opportunity to earn a future payment tied to the level of achievement with respect to one or more performance criteria established by the Administrator for a performance period.

(a) Cash Award. Each Cash Award shall contain provisions regarding (i) the performance goal or goals and maximum amount payable to the Participant as a Cash Award; (ii) the performance criteria and level of achievement versus these criteria that shall determine the amount of such payment; (iii) the period as to which performance shall be measured for establishing the amount of any payment; (iv) the timing of any payment earned by virtue of performance; (v) restrictions on the alienation or transfer of the Cash Award before actual payment; (vi) forfeiture provisions; and (vii) such further terms and conditions, in each case not inconsistent with the Plan, as may be determined from time to time by the Administrator. The maximum amount payable as a Cash Award that is settled for cash may be a multiple of the target amount payable, but the maximum amount payable pursuant to that portion of a Cash Award granted under this Plan for any fiscal year to any Awardee that is intended to satisfy the requirements for "performance-based compensation" under Section 162(m) of the Code shall not exceed $1,000,000.

(b) Performance Criteria. The Administrator shall establish the performance criteria and level of achievement versus these criteria that shall determine

the target and the minimum and maximum amount payable under a Cash Award, which criteria may be based on financial performance or personal performance evaluations or both. The Administrator may specify the percentage of the target Cash Award that is intended to satisfy the requirements for "performance-based compensation" under Section 162(m) of the Code. Notwithstanding anything to the contrary herein, the performance criteria for any portion of a Cash Award that is intended to satisfy the requirements for "performance-based compensation" under Section 162(m) of the Code shall be a measure established by the Administrator based on one or more Qualifying Performance Criteria selected by the Administrator and specified in writing.

(c) Timing and Form of Payment. The Administrator shall determine the timing of payment of any Cash Award. The Administrator may specify the form of payment of Cash Awards, which may be cash or other property, or may provide for an Awardee to have the option for his or her Cash Award, or such portion thereof as the Administrator may specify, to be paid in whole or in part in cash or other property.

(d) Termination of Service. The Administrator shall have the discretion to determine the effect of a Termination of Service on any Cash Award due to (i) disability, (ii) retirement, (iii) death, (iv) participation in a voluntary severance program, or (v) participation in a work force restructuring.

14. Other Provisions Applicable to Awards.

(a) Non-Transferability of Awards. Unless determined otherwise by the Administrator, an Award may not be sold, pledged, assigned, hypothecated, transferred, or disposed of in any manner other than by will or by the laws of descent and distribution, and may be exercised, during the lifetime of the Participant, only by the Participant. If the Administrator makes an Award transferable, either at the time of grant or thereafter, such Award shall contain such additional terms and conditions as the Administrator deems appropriate, and any transferee shall be bound by such terms upon acceptance of such transfer.

(b) Qualifying Performance Criteria. For purposes of this Plan, the term "Qualifying Performance Criteria" shall mean any one or more of the following performance criteria, applied to either the Company as a whole or to a business unit, Affiliate, Related Corporations, or business segment, either individually, alternatively, or in any combination, and measured either annually or cumulatively over a period of years, on an absolute basis or relative to a pre-established target, to previous years' results or to a designated comparison group, in each case as specified in the Award by the Committee: (i) cash flow, (ii) earnings (including gross margin, earnings before interest and taxes, earnings before taxes, and net earnings), (iii) earnings per share, (iv) growth in earnings or earnings per share, (v) stock price, (vi) return on equity or average stockholders' equity, (vii) total stockholder return, (viii) return on capital, (ix) return on assets or net assets, (x) return on investment, (xi) revenue, (xii) income or net income, (xiii) operating income or net operating income, (xiv) operating profit or net operating profit, (xv) operating margin, (xvi) return on operating revenue, (xvii) market share, (xviii) contract awards or backlog, (xix) overhead or other expense reduction, (xx) growth in stockholder value relative to the moving average of the S&P 500 Index or a peer group index, (xxi) credit rating, (xxii) strategic plan development and implementation, (xxiii) improvement

in workforce diversity, (xxiv) EBITDA, and (xxv) any other similar criteria.

(c) Certification. Before payment of any compensation under an Award intended to qualify as "performance-based compensation" under Section 162(m) of the Code, the Committee shall certify the extent to which any Qualifying Performance Criteria and any other material terms under such Award have been satisfied (other than in cases where such relate solely to the increase in the value of the Common Stock).

(d) Discretionary Adjustments Pursuant to Section 162(m). Notwithstanding satisfaction or completion of any Qualifying Performance Criteria, to the extent specified at the time of grant of an Award to "covered employees" within the meaning of Section 162(m) of the Code, the number of Shares, Options or other benefits granted, issued, retained, or vested under an Award on account of satisfaction of such Qualifying Performance Criteria may be reduced by the Committee on the basis of such further considerations as the Committee in its sole discretion shall determine.

(e) Section 409A. Notwithstanding anything in the Plan to the contrary, it is the Company's intent that all Awards granted under this Plan comply with Section 409A of the Code, and each Award shall be interpreted in a manner consistent with that intention.

15. Adjustments upon Changes in Capitalization, Dissolution, Merger or Asset Sale.

(a) Changes in Capitalization.

(i) The limitations set forth in Section 3, the number and kind of Shares covered by each outstanding Award, and the price per Share (but not the total price) subject to each outstanding Award shall be proportionally adjusted to prevent dilution or enlargement of rights under the Plan for any change in the outstanding Common Stock subject to the Plan, or subject to any Award, resulting from any stock splits, combination or exchange of Shares, consolidation, spin-off or recapitalization of Shares or any capital adjustment or transaction similar to the foregoing or any distribution to holders of Common Stock other than regular cash dividends.

(ii) The Administrator shall make such adjustment in such manner as it may deem equitable and appropriate, subject to compliance with Applicable Laws. Any determination, substitution or adjustment made by the Administrator under this Section shall be conclusive and binding on all persons. The conversion of any convertible securities of the Company shall not be treated as a transaction requiring any substitution or adjustment under this Section. Except as expressly provided herein, no issuance by the Company of shares of stock of any class, or securities convertible into shares of stock of any class, shall affect, and no adjustment by reason thereof shall be made with respect to, the number or price of Shares subject to an Award.

(b) Dissolution or Liquidation. In the event of the proposed dissolution or liquidation of the Company, the Administrator shall notify each Participant as soon as practicable before the effective date of such proposed transaction. The Administrator in its discretion may provide for an Option to be fully vested

and exercisable until ten days before such proposed transaction. In addition, the Administrator may provide that any restrictions on any Award shall lapse before the proposed transaction, provided the proposed dissolution or liquidation takes place at the time and in the manner contemplated. To the extent it has not been previously exercised, an Award will terminate immediately before the consummation of such proposed transaction.

(c) Change in Control. If there is a Change in Control of the Company, as determined by the Board or a Committee, the Board or Committee, or board of directors of any surviving entity or acquiring entity may, in its discretion, (i) provide for the assumption, continuation or substitution (including an award to acquire substantially the same type of consideration paid to the stockholders in the transaction in which the Change in Control occurs) of, or adjustment to, all or any part of the Awards; (ii) accelerate the vesting of all or any part of the Options and SARs and terminate any restrictions on all or any part of the Stock Awards or Cash Awards; (iii) provide for the cancellation of all or any part of the Awards for a cash payment to the Participants; and (iv) provide for the cancellation of all or any part of the Awards as of the closing of the Change in Control; provided, that the Participants are notified that they must exercise or redeem their Awards (including, at the discretion of the Board or Committee, any unvested portion of such Award) at or before the closing of the Change in Control.

16. Amendment and Termination of the Plan.

(a) Amendment and Termination. The Administrator may amend, alter, or discontinue the Plan or any Award Agreement, but any such amendment shall be subject to approval of the stockholders of the Company in the manner and to the extent required by Applicable Law.

(b) Effect of Amendment or Termination. No amendment, suspension, or termination of the Plan shall materially impair the rights of any Award, unless agreed otherwise between the Participant and the Administrator. Termination of the Plan shall not affect the Administrator's ability to exercise the powers granted to it hereunder with respect to Awards granted under the Plan before the date of such termination.

(c) Effect of the Plan on Other Arrangements. Neither the adoption of the Plan by the Board or a Committee nor the submission of the Plan to the stockholders of the Company for approval shall be construed as creating any limitations on the power of the Board or any Committee to adopt such other incentive arrangements as it or they may deem desirable, including the granting of restricted stock or stock options otherwise than under the Plan, and such arrangements may be either generally applicable or applicable only in specific cases.

17. Designation of Beneficiary.

(a) An Awardee may file a written designation of a beneficiary who is to receive the Awardee's rights pursuant to Awardee's Award or the Awardee may include his or her Awards in an omnibus beneficiary designation for all rights under the Awardee's Awards

and all benefits under the Plan. To the extent that Awardee has completed a designation of beneficiary such beneficiary designation shall remain in effect with respect to any Award hereunder until changed by the Awardee to the extent enforceable under Applicable Law.

(b) The Awardee may change such designation of beneficiary at any time by written notice. If an Awardee dies and no beneficiary is validly designated under the Plan who is living at the time of such Awardee's death, the Company shall allow the executor or administrator of the estate of the Awardee to receive the Awardee's rights under the Awardee's Awards and all benefits under the Plan, or if no such executor or administrator has been appointed (to the knowledge of the Company), the Company, in its discretion, may allow the spouse or one or more dependents or relatives of the Awardee to receive the Awardee's rights under the Awardee's Awards and all benefits under the Plan to the extent permissible under Applicable Law.

18. No Right to Awards or to Service. No person shall have any claim or right to be granted an Award and the grant of any Award shall not be construed as giving an Awardee the right to continue in the service of the Company or its Affiliates. Further, the Company and its Affiliates expressly reserve the right, at any time, to dismiss any Service Provider or Awardee at any time without liability or any claim under the Plan, except as provided herein or in any Award Agreement entered into hereunder.

19. Preemptive Rights. No Shares will be issued under the Plan in violation of any preemptive rights held by any stockholder of the Company.

20. Legal Compliance. No Share will be issued pursuant to an Award under the Plan unless the issuance and delivery of such Share, as well as the exercise of such Award, if applicable, will comply with Applicable Laws. Issuance of Shares under the Plan shall be subject to the approval of counsel for the Company with respect to such compliance. Notwithstanding anything in the Plan to the contrary, the Plan is intended to comply with the requirements of Section 409A of the Code and shall be interpreted in a manner consistent with that intention.

21. Inability to Obtain Authority. To the extent the Company is unable to or the Administrator deems that it is not feasible to obtain authority from any regulatory body having jurisdiction, which authority is deemed by the Company's counsel to be necessary to the lawful issuance and sale of any Shares hereunder, the Company shall be relieved of any liability with respect to the failure to issue or sell such Shares as to which such requisite authority shall not have been obtained.

22. Reservation of Shares. The Company, during the term of this Plan, will at all times reserve and keep available such number of Shares as shall be sufficient to satisfy the requirements of the Plan.

23. Notice. Any written notice to the Company required by any provisions of this Plan shall be addressed to the Secretary of the Company and shall be effective when received.

24. Governing Law; Interpretation of Plan and Awards.

(a) This Plan and all determinations made and actions taken pursuant hereto shall be governed by the substantive laws, but not the choice of law rules, of the state of New York.

(b) If any provision of the Plan or any Award granted under the Plan is declared to be illegal, invalid, or otherwise unenforceable by a court of competent

jurisdiction, such provision shall be reformed, if possible, to the extent necessary to render it legal, valid, and enforceable, or otherwise deleted, and the remainder of the terms of the Plan and Award shall not be affected except to the extent necessary to reform or delete such illegal, invalid, or unenforceable provision.

(c) The headings preceding the text of the sections hereof are inserted solely for convenience of reference, and shall not constitute a part of the Plan, nor shall they affect its meaning, construction or effect.

(d) The terms of the Plan and any Award shall inure to the benefit of and be binding upon the parties hereto and their respective permitted heirs, beneficiaries, successors, and assigns.

(e) All questions arising under the Plan or under any Award shall be decided by the Administrator in its total and absolute discretion. If the Participant believes that a decision by the Administrator with respect to such person was arbitrary or capricious, the Participant may request arbitration with respect to such decision. The review by the arbitrator shall be limited to determining whether the Administrator's decision was arbitrary or capricious. This arbitration shall be the sole and exclusive review permitted of the Administrator's decision, and the Awardee shall as a condition to the receipt of an Award be deemed to waive explicitly any right to judicial review.

25. Limitation on Liability. The Company and any Affiliate or Related Corporation that is in existence or hereafter comes into existence shall not be liable to a Participant, an Employee, an Awardee, or any other persons as to:

(a) The Non-Issuance of Shares. The non-issuance or sale of Shares as to which the Company has been unable to obtain from any regulatory body having jurisdiction the authority deemed by the Company's counsel to be necessary to the lawful issuance and sale of any shares hereunder; and

(b) Tax Consequences. Any tax consequence expected, but not realized, by any Participant, Employee, Awardee or other person due to the receipt, exercise or settlement of any Option or other Award granted hereunder.

26. Unfunded Plan. Insofar as it provides for Awards, the Plan shall be unfunded. Although bookkeeping accounts may be established with respect to Awardees who are granted Stock Awards under this Plan, any such accounts will be used merely as a bookkeeping convenience. The Company shall not be required to segregate any assets that may at any time be represented by Awards, nor shall this Plan be construed as providing for such segregation, nor shall the Company or the Administrator be deemed a trustee of stock or cash to be awarded under the Plan. Any liability of the Company to any Participant with respect to an Award shall be based solely upon any contractual obligations that may be created by the Plan; no such obligation of the Company shall be deemed secured by any pledge or other encumbrance on any property of the Company. Neither the Company nor the Administrator shall be required to give any security or bond for the performance of any obligation that may be created by this Plan.

IN WITNESS WHEREOF, the Company, by its duly authorized officer, has executed this Plan, effective as of November 15, 2006.

RADNET, INC.

By: /s/ Howard G. Berger, M.D.
Its: Chief Executive Officer and President

AMENDMENT NO. 1 TO THE 2006 EQUITY INCENTIVE PLAN

RadNet, Inc. (the "Company") hereby amends its 2006 Equity Incentive Plan (the "Plan"), retroactively effective as of the Plan's original adoption, as follows:

The second sentence of Section 3(b) of the Plan is hereby amended in its entirety to read as follows:

Notwithstanding anything to the contrary in the Plan, the limitations set forth in this Section 3(b) shall (i) not apply to any Award that is not intended to qualify as "performance-based compensation" within the meaning of Section 162(m) of the Code, or (ii) be subject to adjustment under Section 15 of the Plan only to the extent that such adjustment will not affect the status of any Award intended to qualify as "performance-based compensation" under Section 162(m) of the Code.

The Company has caused this Amendment No. 1 to be signed on the date indicated below, to be effective as indicated above.

	RADNET, INC.
Dated: August 7, 2008	By: /s/ Howard G. Berger, M.D. Its: Chief Executive Officer and President

ANNUAL MEETING OF STOCKHOLDERS OF

RADNET, INC.

JUNE 5, 2009

NOTICE OF INTERNET AVAILABILITY OF PROXY MATERIAL:
The Notice of Meeting, proxy statement and proxy card
are available at - http://www.proxyvote.com

Please sign, date and mail your proxy card in the envelope provided as soon as possible.

Please detach along perforated line and mail in the envelope provided.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE "FOR" PROPOSALS NO. 1, 2, 3 and 4. PLEASE SIGN, DATE AND RETURN PROMPTLY IN THE ENCLOSED ENVELOPE. PLEASE MARK YOUR VOTE IN BLUE OR BLACK INK AS SHOWN HERE x

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1. To elect the following seven persons (except as marked to the contrary) as directors of the Company for a one-year term, or until their successors are duly elected and qualified:

NOMINEES

o FOR ALL NOMINEES

o WITHHOLD AUTHORITY

m Howard G. Berger, M.D.
m Marvin S. Cadwell
m John V. Crues, III, M.D.

	FOR	AGAINST	ABSTA
2. To amend the 2006 Equity Incentive Plan to increase the number of shares available to 6,500,000.	o	o	o
3. To ratify the selection of Ernst & Young LLP as the Company's independent registered public accounting firm for the year ending December 31, 2009.	o	o	o

	m Norman R. Hames				
FOR ALL NOMINEES	m Lawrence L. Levitt	4. To transact any other business that may properly come before the meeting or any adjournment or postponement of the meeting.	o	o	o
	m Michael L. Sherman, M.D.				
o FOR ALL EXCEPT (See instructions below)	m David L Swartz				

THIS PROXY IS REVOCABLE AND WILL B VOTED AS DIRECTED BY THE UNDERSIGNED BELOW. Where no choice is specified, this proxy card will be voted FOR suc proposal where no vote is specified.

INSTRUCTIONS: To withhold authority to vote for any individual nominee(s), mark "FOR ALL EXCEPT" and fill in the circle next to each nominee you wish to withhold, as shown here.

Please consider the issues discussed in the proxy statement and cast your vote by completing, dating, signing and mailing the proxy card in th postage-paid envelope included with the proxy statement.

Stockholders holding shares with a broker, bank other nominee may also be eligible to vote via t Internet or to vote telephonically if their broker, bank or other nominee participates in the proxy voting program provided by Broadridge Financi Solutions, Inc. Please consult the instruction for received from your broker or bank.

To change the address on your account, please check the box at right and indicate your new address in the address space above. o
Please note that changes to the registered name(s) on the account may not be submitted via this method.

Signature of Stockholder	Date	Signature of Stockholder	Date

Note: Please sign exactly as your name or names appear on this Proxy. When shares are held jointly, each holder should sign. When signing as executor, administrator, attorney, trustee or guardian, please give full title as such. If the signer is a corporation, please sign full corporate name by a duly authorized officer, giving full title as such. If signer is a partnership, please sign in partnership name by authorized person.

PROXY

RADNET, INC.

THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS
FOR THE ANNUAL MEETING OF STOCKHOLDERS
JUNE 5, 2009

The undersigned hereby appoints Mark Stolper and Jeffrey Linden, or any one of them, and each with full power of substitution, to act as attorneys and proxies for the undersigned to attend the Annual Meeting of Stockholders of the Company to be held at The Olympic Collection, 11301 Olympic Blvd., Los Angeles, California on June 5, 2009 at 10:00 a.m. (Pacific Time) and any adjournments or postponements thereof, to cast on behalf of the undersigned all votes that the undersigned is entitled to cast at such meeting and otherwise to represent the undersigned at the meeting with all powers possessed by the undersigned if personally at the meeting. The undersigned acknowledges receipt from the Company prior to the execution of this proxy of a Notice of Annual Meeting of Stockholders and a Proxy Statement, the terms of which are incorporated herein by reference, and revokes any proxy heretofore given in respect to such meeting.

THE VOTES ENTITLED TO BE CAST BY THE UNDERSIGNED WILL BE CAST AS INSTRUCTED HEREIN. IF THIS PROXY IS EXECUTED BUT NO INSTRUCTION IS GIVEN, THE VOTES ENTITLED TO BE CAST BY THE UNDERSIGNED WILL BE CAST "FOR" PROPOSALS 1, 2, 3 AND 4.

(Continued and to be signed on the reverse side)