



Bristol-Myers Squibb

2005 Annual Report

Every hour. Everywhere.

A day in the life of Bristol-Myers Squibb



The Bristol-Myers Squibb Mission

Our company's mission is to extend and enhance human life by providing the highest-quality pharmaceutical and related health care products.

We pledge—to our patients and customers, to our employees and partners, to our shareholders and neighbors, and to the world we serve—to act on our belief that the priceless ingredient of every product is the honor and integrity of its maker.



On the cover

HOMESTEAD, FLORIDA When Dixie Dixon was born, doctors learned that she had a hole in her heart. Dixie's pediatrician recommended that her mom try to keep Dixie from crying and getting overworked. And because Dixie had colic, he also suggested Mead Johnson's *Nutramigen LIPIL*, a hypoallergenic infant formula designed to help babies with colic due to cow's milk allergy. Since Dixie began taking *Nutramigen LIPIL*, the colic has disappeared. Says her mom, "Dixie's a very determined little girl." (see story, page 25)

Mead Johnson Nutritionals is a world leader in nutrition, and since its founding in 1905 has been dedicated to providing infants and children with the best start in life. The year 2005—Mead Johnson's centennial—was a banner year for the company, with sales of more than \$2 billion due to strong growth in U.S. and international markets. Mead Johnson's *Enfamil* infant formulas constitute Bristol-Myers Squibb's third-largest brand.



To Our Stockholders

Approximately four years ago, we began executing a strategy to transform our company in several important ways. We sharpened the focus of our pharmaceutical business on a defined set of serious diseases with significant unmet medical need. We're addressing this need with innovative medications that are largely coming from our own research and development organization—a meaningful change from the past. And we're acting to meet the wider needs of society, by expanding access to medicines and building critically needed health care infrastructure in parts of the developing world that are afflicted by disease and poverty.

Our goal is to continue to realize our mission of extending and enhancing life well into the future in a way that builds sustainable long-term growth and leadership for our company. Most importantly—through our commitment to focus, innovation and compassion—we want to provide new hope and help for patients facing serious health challenges.

Over the past 12 to 15 months, we've achieved several important milestones as we have continued to execute our strategy:

- Our medications are helping millions of patients battling schizophrenia and other psychiatric disorders, HIV/AIDS, cancer, chronic hepatitis B, rheumatoid arthritis, atherosclerosis/thrombosis, hypertension and other serious diseases.
- Global sales of several of our key pharmaceutical products increased at double-digit rates in 2005, building on strong gains from previous years. These growth products now account for nearly half of our worldwide pharmaceutical sales.
- Our Health Care businesses—which collectively contributed more than 20 percent of our net sales and more than 30 percent of operating earnings in 2005—again delivered good growth and provided important stability.
- Three drugs gained regulatory approval, representing our fourth, fifth and sixth new medications since November 2002. No pharmaceutical company had more new drugs (“new molecular entities”) approved in the U.S. between November 2002 and December 2005.
- In our new product pipeline, we advanced two compounds to Phase III development and submitted for regulatory review a promising anti-cancer compound that we hope will become our seventh new medicine.
- We're putting significant additional resources behind our new product launches and our pipeline, including investing hundreds of millions of dollars in our biologics capabilities.
- We're continuing to strengthen our culture by holding ourselves accountable to the highest standards of integrity, ethical behavior and professionalism, further developing our processes and mechanisms related to compliance and good corporate citizenship.
- We broke new ground in our philanthropic efforts, funding the first-ever Pediatric AIDS Corps of physicians for Africa and expanding our global network of pediatric AIDS clinics in the developing world.



James D. Robinson III (right)
Chairman of the Board

Peter R. Dolan
Chief Executive Officer

Financial Performance

In 2005, Bristol-Myers Squibb earned \$3.0 billion, or \$1.52 per diluted share, on a GAAP basis, on total net sales of \$19.2 billion from continuing operations. On a non-GAAP basis, excluding specified items, total net earnings from continuing operations were \$2.8 billion, or \$1.43 per diluted share.

Our sales and earnings performance was affected by the significant transition under way in our pharmaceutical portfolio. Our growth drivers—including Abilify, for schizophrenia and acute bipolar mania; *Reyataz*, for HIV; Erbitux, for cancer; Plavix, to inhibit platelet aggregation; and Avapro/Avalide, for hypertension—continued to replace older products losing exclusivity. In the case of our largest product, Plavix, and our three newer medications, Abilify, Erbitux and *Reyataz*, global sales or revenue increased 15 percent, 54 percent, 58 percent and 68 percent, respectively. However, their growth was offset by declining sales of products losing exclusivity. As a result, our total net sales for the year declined slightly.

As expected, non-GAAP earnings were lower in 2005. This largely reflects an important strategic

decision we made a few years back to increase investments behind our pipeline and growth drivers, even as our margins were coming under pressure due to our new mix of products. We knew there would be some short-term negative impact on our performance with this approach, but we believed—and still believe—that investing in our long-term future was and is the right choice to make.

While pharmaceuticals remain our largest business, our three Health Care businesses continue to contribute significantly to both the company's mission and its financial performance. Mead Johnson Nutritionals—the world's leading producer of infant formula—delivered sales well in excess of \$2 billion in 2005, with double-digit growth in both revenue and earnings. Sales of ConvaTec's wound therapeutics line and Medical Imaging's cardiovascular imaging agents also increased.

These Health Care businesses provide important strength and stability for the company. For the most part they are not subject to the volatility in sales and earnings associated with the patent cycles of the pharmaceutical industry.

Our medications are extending and enhancing the lives of millions of patients battling schizophrenia and other psychiatric disorders, HIV/AIDS, cancer, chronic hepatitis B, rheumatoid arthritis, atherosclerosis/thrombosis, hypertension and other serious diseases.

Executing Our Strategy

During 2005, we continued to execute our strategy and are largely on track. We launched our fourth new pharmaceutical product since late 2002—*Baraclude*, for chronic hepatitis B—which addresses an area of significant unmet medical need. Hepatitis B is an insidious disease of the liver that can lead to severe health complications, including cancer. We see tremendous possibility for the medicine to help patients all over the world, including China and other parts of Asia, where hepatitis B is a serious and growing health concern.

In early 2006, we are introducing two additional medications. *Orencia* is our new treatment for rheumatoid arthritis. Millions of people around the world suffer from this painful and crippling disease that erodes quality of life and reduces the lifespan of many patients. *Orencia* represents the second of our biologic products. In areas like cancer and autoimmune disorders, biologics are playing an increasingly important role.

Last month, the U.S. Food and Drug Administration (FDA) approved EMSAM, a transdermal patch for treatment of adults with major depressive disorder that we licensed in late 2004 from Somerset Pharmaceuticals. Licensing compounds and technology remains important to the successful execution of our strategy. During 2005, we entered into six research alliances that will help us deliver more near-term development candidates into our pipeline as well as improve our technology base.

We had been hopeful about approval for *Pargluva*, for treatment of type 2 diabetes, which had been submitted to the FDA in 2004 and received a positive advisory committee recommendation last September. The FDA issued an “approvable” letter for *Pargluva* in October, requesting additional information from ongoing clinical trials to further understand the cardiovascular safety profile of the product before a final decision

is made. We have concluded that new long-term studies likely will be required before *Pargluva* can be approved and successfully commercialized. While we are disappointed with this outcome, we will continue to work with the FDA as we study our options. These include conducting additional studies, which may take as long as five years, or terminating further development of the product.

We’re pleased to have a robust group of potential medications in our pipeline. Behind our newest medications are promising late-stage compounds that include dasatinib, for chronic myelogenous leukemia, which is now under review by the FDA. Other compounds in Phase III development include ixabepilone, ipilimumab and vinflunine, for cancer; belatacept, for the prevention of solid organ transplantation rejection; and saxagliptin, for type 2 diabetes.

Baraclude and *Orencia* are addressing two very different serious diseases. Nevertheless, they have one important thing in common: They both were discovered and developed in our company’s own laboratories. Dasatinib, ixabepilone and belatacept are also internally derived compounds. We are pleased that our R&D organization continues to be productive, thanks in large part to its leadership as well as to the talent, dedication and commitment of thousands of scientists and other research staff. This productivity is also tied to our increased investments in R&D in recent years, as part of our strategy. Over the past three years, we have boosted companywide R&D expenditures 11 percent per year on a compounded annual growth rate basis.

To ensure that we have the resources to continue investing in our pipeline opportunities and new product launches, our strategy also commits all of us at Bristol-Myers Squibb to reducing—or at a minimum, holding flat—all expenditures unrelated to our R&D and business

We have made it our priority to build a world-class compliance infrastructure at Bristol-Myers Squibb and, more importantly, to instill within the entire company a culture of integrity, strong values and unwavering commitment to the highest standards of ethical and professional conduct.

priorities. We have realized substantial savings in recent years in such areas as manufacturing, drug development, information technology and our sales force. But we need to do much more to reduce operating costs over the long-term. For this reason, we recently launched a companywide effort to realize \$600 million in additional savings in 2007–2008 by focusing resources and work on high-value priorities, and by further streamlining business processes and decision-making.

We continued to strengthen our senior management team in 2005, consolidating our global pharmaceutical and health care operations under the leadership of two highly experienced executives. Lamberto Andreotti, who most recently headed our international pharmaceuticals and global Mead Johnson Nutritionals and ConvaTec businesses, was promoted to executive vice president of the company and president, Worldwide Pharmaceuticals. Lamberto has been instrumental in the success of several of our important global product launches. John Celentano, formerly president of our Latin America and Canada medicines businesses, was named president of the Health Care Group. Both he and Lamberto have solid records of achievement in growing businesses and expanding markets.

When we communicated our strategy in 2003, we indicated that the next several years would be transitional for the company as our pharmaceutical portfolio continued to evolve. In 2006, exclusivity on *Pravachol*, our second-largest product, will expire in both the U.S. and France, contributing to an expected decline in earnings for the year. As has been the case in the past several years, we expect that the growth of our newer pharmaceutical products—as well as our Health Care businesses—will help mitigate the impact of these exclusivity losses and enable us to continue increasing investments in our pipeline and new products.

Looking ahead, we remain positive about entering a period of earnings and sales growth in 2007. Beginning then, we anticipate relatively few additional significant exclusivity losses for the next several years, and we believe our pipeline and licensing efforts will provide a sustained flow of new products in our disease areas of focus. In addition, as we look to resume growth, it's also important for us to deliver on our productivity targets.

Among other things, this scenario assumes continued exclusivity for Plavix, which is the subject of ongoing litigation. It is our belief that the patent for Plavix is valid and has been infringed, and—together with our partner, Sanofi-Aventis—we are vigorously defending our intellectual property.

Compliance and Corporate Governance

Over the past several years, we've made it our priority to build a world-class compliance infrastructure at Bristol-Myers Squibb and, more importantly, to instill within the entire company a culture of integrity, strong values and unwavering commitment to the highest standards of ethical and professional conduct. In recent years, we've greatly expanded the scope and reach of our compliance organization, and strengthened and implemented policies to report potential compliance incidents, train personnel on compliance issues, protect privacy and appropriately assess and manage business risk.

In June, the company announced that it had resolved an investigation by the U.S. Attorney's Office in New Jersey relating to U.S. wholesaler inventory and various accounting matters, in a Deferred Prosecution Agreement (DPA) with the government. As part of that agreement, we committed to continuing to implement remedial measures previously undertaken, and to take additional measures, including conducting corporate

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we saw a pressing need to provide better treatment and support to the
many children struggling with the disease.

citizenship and corporate financial reporting compliance training, among other actions. Information about our compliance with paragraph 25 of the DPA is contained in the financial review in this report. In addition, the Board of Directors proposed and implemented the separation, at this time, of the positions of chairman and chief executive officer.

Social Responsibility

Bristol-Myers Squibb recognizes the high expectations of honesty and transparency placed on companies in our industry. We have taken the initiative to adopt progressive policies in two areas of particular concern to many in the health care field as well as in the public at large. In June, we announced our new policy on direct-to-consumer (DTC) advertising. Among other commitments, we have voluntarily agreed to forego all DTC advertising of our new products for a period of at least one year following their introduction into the marketplace. Our stated goal is to give physicians and others sufficient time to learn about and understand our new medications before they are promoted to the general public.

More recently, we announced a new policy on disclosure of information from clinical trials. We will disclose the results of any Bristol-Myers Squibb-sponsored clinical trials conducted in patients, regardless of development phase or outcome, for the company's marketed medicines. At the time of launch of our new medicines, we will post the results or reference the publication status for completed clinical trials conducted in patients. We also will disclose, on a timely basis, the results of all Bristol-Myers Squibb-sponsored clinical trials in patients that complete post-launch.

In addition to transparency, access to medicines is of great concern. In 2005, the company intensified its efforts in this area, including taking a leadership

role in an initiative of the industry's trade association, the Pharmaceutical Research and Manufacturers of America (PhRMA), to make it easier for people in need to obtain their medications free of charge or at deeply discounted prices.

We were an early proponent of the PhRMA-sponsored Partnership for Prescription Assistance, launched last April, which links over 475 access programs across the U.S. and already has helped more than 1.6 million people. In addition, through our company's own access program—one of the oldest and most generous in the industry—we provided more than \$600 million in free medicines in 2005 to more than 800,000 people.

Bristol-Myers Squibb also broke new ground in its philanthropic programs focused on the HIV/AIDS crisis in sub-Saharan Africa. With HIV/AIDS claiming on average the life of one child in Africa every minute, we saw a pressing need to provide better treatment and support to the many children struggling with this disease.

Building on the success over the past three years of our pediatric AIDS clinic in Botswana—which has treated thousands of children and their families and is one of the largest pediatric HIV/AIDS treatment centers in the world—we recently opened two centers, in Lesotho and Swaziland, where an estimated 36,000 children are infected with HIV. We also announced that centers will be built in the African countries of Uganda and Burkina Faso, and in China.

Our partners in this global project are the Baylor College of Medicine, which is staffing the centers and providing critical technical support, and host-country governments. In 2005, we joined with Baylor to fund a new initiative, the Pediatric AIDS Corps, comprising 250 pediatricians and family practitioners who will work in our treatment clinics as well as in remote areas of Africa, where good medical care is scarce. Corps doctors have

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begun assuming their duties in the region, and eventually hope to treat as many as 80,000 children. They also will train local health care practitioners to provide the specialized care that children with HIV require.

Focus, Innovation, Compassion

As we move forward with a strategy to transform our company into a health care leader for the future, our guiding principles and values remain unchanged. They are outlined in the Bristol-Myers Squibb mission—to extend and enhance human life—and in our Pledge to our shareholders and indeed to all of our stakeholders: “To act on our belief that the priceless ingredient of every product is the honor and integrity of its maker.” By focusing on areas of significant unmet medical need, by providing innovative medications and other health care products, and by reaching out to people in need—we believe we can go even further toward realizing our mission and living up to our ideals.

Indeed, we see focus, innovation and compassion as the defining characteristics of our company as we seek to create a unique place in the health care world of tomorrow. Together, these three ideas express a deep commitment to helping patients that goes beyond the narrow boundaries of commercial relationships. Simply stated, our goal—through the products we make, the causes we support and the values we uphold—is to help people live better lives—to give people the power to prevail in the face of disease.

As you’ll see in this report, every hour of every day, Bristol-Myers Squibb is touching a life somewhere in the world. For our 42,000 employees, this reality brings both a sense of personal satisfaction and a recognition of tremendous responsibility. Certainly, there are challenges ahead—for our company as well as our industry. After all, we operate in an industry full of risk and uncer-

tainty. But the opportunities ahead to fight disease and make a significant difference in people’s lives have never been more promising. We’re fully prepared to seize those opportunities—by building a hopeful future of better health for people everywhere, and a successful future of growth and leadership for Bristol-Myers Squibb.

Finally, we would like to thank our dedicated employees for their outstanding work on behalf of our mission, our patients and our company. We also are grateful to the rest of the Board of Directors for their ongoing commitment and support. Special thanks are owed to Ellen Futter—who recently retired from the Board—and to Louis Gerstner and Louis Sullivan, who plan to retire on May 2. They have contributed greatly to the company’s achievements and progress over the years. In addition, we’re pleased to welcome to the Board Louis Freeh, former vice chairman and general counsel, MBNA America Bank, N.A.

On a personal note, it’s been a pleasure and honor for us to continue working so closely and productively together on the important issues facing our company. Together with all the people of Bristol-Myers Squibb, we are thankful for the many unique opportunities we have—through our business, research and philanthropy—to have a lasting and positive influence on the world.



James D. Robinson III
Chairman of the Board



Peter R. Dolan
Chief Executive Officer

March 13, 2006

2005 BUSINESS HIGHLIGHTS

Creating a World of Difference

Plavix **#2** **WORLDWIDE***
BRAND

02.03.05 - Bristol-Myers Squibb ranks among the world's 100 Most Sustainable Corporations at the World Economic Forum.

Among the WORLD'S
top100
SUSTAINABLE
CORPORATIONS

2005

JANUARY

FEBRUARY

MARCH

APRIL

01.11.05 - Together Rx Access Card offers savings at the pharmacy counter to Americans with no prescription drug coverage.

01.13.05 - Construction begins on Swaziland's first pediatric HIV/AIDS medical center, with funding provided by Bristol-Myers Squibb.

01.13.05 - Global development and commercialization collaboration with Medarex Inc. becomes effective for ipilimumab, in development for the treatment of metastatic melanoma.

03.16.05 - ConvaTec receives Technology Innovation and Leadership of the Year award from Frost & Sullivan.

03.22.05 - Bristol-Myers Squibb extends relief efforts to state-administered AIDS Drug Assistance Programs, ensuring that thousands of low-income people living with HIV/AIDS have access to medications.

03.29.05 - U.S. Food and Drug Administration (FDA) approves *Baraclude* (entecavir) for treatment of chronic hepatitis B virus infection.

04.05.05 - Company joins Partnership for Prescription Assistance, a national program to help uninsured Americans get their prescription medications.

04.21.05 - Bristol-Myers Squibb Medical Imaging announces award of three-year contract to offer *Definity* to 1,500 hospitals and other affiliated health care sites.

*IMS Health worldwide sales data for year 2005.

3 of industry's top 10
RECENT
PRODUCT
LAUNCHES

ABILIFY • ERBITUX • REYATAZ

Mead Johnson \$2 Billion in Sales

05.11.05 - Bristol-Myers Squibb completes sale of Oncology Therapeutics Network to One Equity Partners LLC.

05.13.05 - Bristol-Myers Squibb wins Team of the Year Award from Pharmaceutical Manufacturing magazine, recognizing efficiency and quality at manufacturing sites.

07.11.05 - ConvaTec launches Aloe Vesta Protective Barrier Spray.

07.21.05 - ConvaTec researchers receive 2005 Manuscript Award from Journal of Wound, Ostomy and Continence Nursing.

Bristol-Myers Squibb

MEDICAL IMAGING

A global leader in cardiovascular imaging

MAY

JUNE

JULY

AUGUST

06.13.05 - Bristol-Myers Squibb announces its Direct-To-Consumer (DTC) Communications Code, including a pledge to refrain from DTC branded mass media advertising for at least 12 months following a new drug launch.

06.22.05 - Bristol-Myers Squibb signs manufacturing agreement with Celltrion to produce select biologic products.

06.27.05 - Bristol-Myers Squibb and Baylor College of Medicine announce plans to create a new Pediatric AIDS Corps for Africa.

FIRST TO
VOLUNTARILY FOREGO
DTC Ads
DURING A NEW
DRUG'S FIRST YEAR
ON MARKET

08.01.05 - Company ranks among top charitable contributors, according to the Chronicle of Philanthropy.

08.10.05 - Mead Johnson Nutritionals launches *Enfamil Gentlease LIPIL* infant formula.

08.30.05 - Company receives Puerto Rico Manufacturers Association Security award.

08.30.05 - ImClone Systems Incorporated and Bristol-Myers Squibb file supplemental application for Erbitux (cetuximab) for treatment of head and neck cancer.

08.31.05 - Bristol-Myers Squibb completes sale of U.S. and Canadian consumer medicines business to Novartis AG.

#1 ConvaTec IN INNOVATION

Top 10
Company
for Working
Mothers

09.13.05 - Working Mother magazine names Bristol-Myers Squibb one of the 10 Best Companies for Working Mothers for the fifth consecutive year.

09.20.05 - Company promotes Lamberto Andreotti to executive vice president and president, Worldwide Pharmaceuticals.

09.27.05 - Bristol-Myers Squibb receives Community award for *SECURE THE FUTURE* from the Global Business Coalition on HIV/AIDS.

09.29.05 - Bristol-Myers Squibb *Tour of Hope* kicks off in San Diego as transcontinental bike ride raises awareness of cancer clinical trials.

11.16.05 - *Baraclude* receives marketing approval in China.

11.29.05 - Mead Johnson celebrates its centennial.

SEPTEMBER

OCTOBER

NOVEMBER

DECEMBER

10.18.05 - FDA issues approvable letter for *Pargluva* (muraglitazar) and requests additional safety data. Bristol-Myers Squibb studies its options.

10.31.05 - Bristol-Myers Squibb agrees to develop certain HIV medicines and grant royalty-free license to nonprofit group for use in developing countries.

12.01.05 - Lesotho's first children's HIV/AIDS medical center opens, funded by Bristol-Myers Squibb and operated by Baylor College of Medicine.

12.02.05 - Company promotes John E. Celentano to president, Health Care Group.

12.06.05 - Bristol-Myers Squibb and Exelixis Inc. agree to develop novel cardiovascular disease treatments.

12.15.05 - DiversityBusiness.com names Bristol-Myers Squibb among America's top organizations for multicultural business opportunities for sixth consecutive year.

12.23.05 - FDA approves *Orencia* (abatacept) for treatment of rheumatoid arthritis.

12.28.05 - Bristol-Myers Squibb completes FDA application for approval of dasatinib for treatment of chronic myelogenous leukemia.

BRISTOL-MYERS SQUIBB

opens treatment centers
focusing on children with

HIV/AIDS

in Africa

THE FUTURE

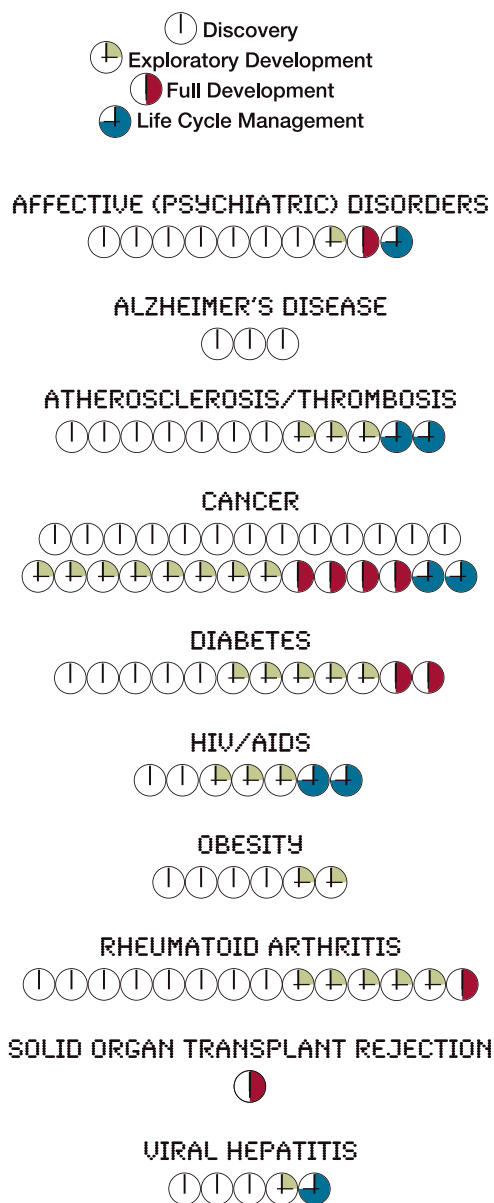
A Pipeline OF HOPE

BRISTOL-MYERS SQUIBB researchers are dedicated to discovering and developing innovative medicines that address serious unmet medical need in key disease areas. Those areas, listed in the chart below, were selected with an emphasis on where there remain significant patient needs as well as opportunities for leadership by the company.

Compounds and research programs in **DISCOVERY** are at the earliest stages of research. Compounds in **EXPLORATORY DEVELOPMENT** are in preclinical or early clinical development. **FULL DEVELOPMENT** compounds are investigational drugs that have been submitted to regulatory agencies for approval or are in late-stage clinical development. **LIFE CYCLE MANAGEMENT** compounds are among approved medicines that are driving current and future growth while continuing their clinical development to determine whether additional indications and formulations will benefit patients.

Each investigational compound or research program is represented in the chart as a clock indicating its stage of development: 12 o'clock for Discovery, 3 o'clock for Exploratory Development, 6 o'clock for Full Development and 9 o'clock for Life Cycle Management. Some of the compounds are discussed in the Special Report beginning on page 11.

Throughout this report, we call attention to the importance of our ongoing clinical trials and we highlight responses from



Pipeline chart as of January 2006.

some of our individual clinical trial patients.

While results may be unpredictable for any one participant in an individual experimental study, these personal accounts illustrate the importance of participation in clinical trials, which are essential to the development of the next generation of medical innovation. The true test of whether we can turn hope into a reality for patients is whether we can document a real clinical benefit across a significant number of research participants.

Our ability to bring new products to patients in need or to find new uses for our current products is dependent upon our demonstrating safety and effectiveness and a favorable benefit-risk relationship via systematic testing in patients who volunteer to participate in our studies.

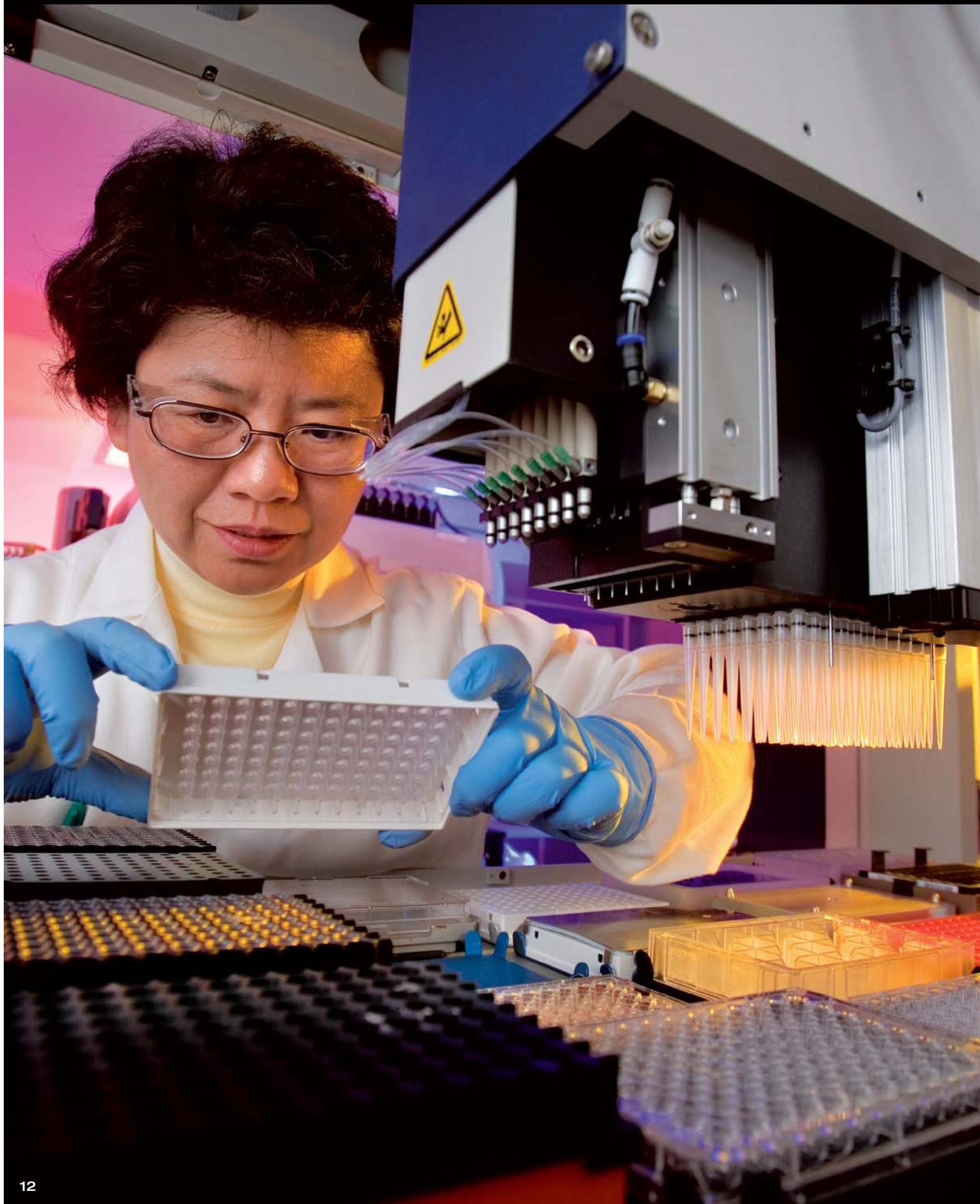
Like any other scientific endeavor, clinical testing of novel drug compounds is a complex, time-consuming, resource-intensive process with no guaranteed results. But, as described here, Bristol-Myers Squibb is committed to pursuing such clinical development and, in doing so, to bringing new hope to patients.

Every hour. Everywhere.

Every hour of every day, somewhere around the world, we at Bristol-Myers Squibb are helping to make a difference in people's lives. From Brooklyn to Beijing and from Illinois to Indonesia, we are fulfilling our mission to extend and enhance human life through the products we make, the science we pursue and the programs we support.

In this special report, we invite you to travel with us around the world as well as around the clock. On this journey we will visit some of those whose lives we have touched—like Melanie Smith of Hayes, England; Eduardo Marafanti of São Paulo, Brazil; and Rob Hill of Vancouver, British Columbia. The lives of these people were once defined and limited by illness. Now they—and millions of others—are pursuing their dreams.

8:10 AM HOPEWELL, NEW JERSEY





Discovery R&D

Sustaining the flow

To build and sustain a robust pipeline of new medications now and well into the future, Bristol-Myers Squibb leaves no stone unturned.

“We’re continuously working to select the right targets and synthesize the right compounds to help enhance development success rates,” says Francis Cuss, M.D., F.R.C.P., senior vice president, Drug Discovery. “We’ve achieved a great deal in these areas with new processes, new tools and new technologies, but the greatest impact has been through our scientists’ innovative thinking and cutting-edge research.”

The company’s Discovery group feeds a steady stream of novel compounds into the development pipeline in order to find innovative therapies in areas of significant unmet medical need. Selected for development in 2005, for example, were drug candidates in atherothrombosis, cancer, diabetes, HIV/AIDS, obesity and rheumatoid arthritis.

External alliances also provide potential development candidates. New collaborations in 2005 may one day lead to additional medications for atherosclerosis, autoimmune diseases, cancer, coronary artery disease and transplantation. Other partnerships provide enabling technologies to advance the company’s screening, biomarker and pharmacogenomic efforts that help enable medications to target specific patient populations.

“As a result of these efforts,” says Cuss, “our early development success rate is probably the best in our history.”



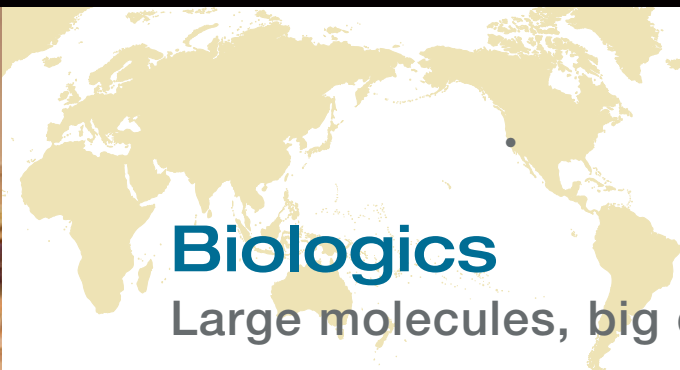
7:00 AM WALLINGFORD, CONNECTICUT

It’s already early in the morning, and Kingsley Appiah, research scientist in Lead Discovery (left), and Jonathan O’Connell, Ph.D., group leader, are examining a microtiter plate containing more than 350 compounds for screening against a specific disease target. Utilizing advanced robotic technology, Bristol-Myers Squibb may screen up to 150,000 compounds a day from a library of millions of compounds. “High-throughput screening is one of our key tools in the early stages of drug discovery,” says O’Connell. “We hope to find biological activity among the compounds in order to find drug leads in each of our disease areas.”

8:10 AM HOPEWELL, NEW JERSEY

An hour later, at the company’s Applied Genomic labs, Aiqing He, senior research scientist (facing page), examines high-throughput array plates as she tests potential novel treatments for metabolic diseases. Each plate contains 96 gene chips, and each chip contains 600,000 genetic features. “This technology helps us determine whether a drug is specifically hitting the right target,” says He. “As a result, we can design drugs to maximize their potential effectiveness and minimize potential side effects.”





Biologics

Large molecules, big difference

Most medicines today are compounds known as small molecules. But now a new kind of compound is delivering to patients an increasing number of novel and targeted treatments. They're called large molecules, also known as biologics. At Bristol-Myers Squibb, two biologics—Erbix (cetuximab), for certain patients with metastatic colorectal cancer and for the treatment of squamous cell head and neck cancer, and *Orencia* (abatacept), for those with rheumatoid arthritis—are leading the way.

Large molecules are aptly named. They can be 200 or more times the size of small molecules. Often designed to bind to specific cell surface receptors—which are themselves large molecules—biologics are generally more targeted than traditional small molecule drugs.

“As much as 25 percent of major new therapies in the future are anticipated to be biologics,” says Mark Powell, Ph.D., senior vice president of the Pharmaceutical Development Center of Excellence. “We recognize the great potential for these compounds to treat a wide variety of diseases, and we are accelerating our large molecule capabilities through technology acquisitions, licensing opportunities and our own development programs.”

Erbix, the company's first marketed biologic, was developed by Bristol-Myers Squibb and ImClone Systems Incorporated. *Orencia*, approved in December 2005, is the first marketed biologic compound discovered by Bristol-Myers Squibb. The company has a pipeline of other biologic compounds in development, including belatacept, for the prevention of solid organ transplant rejection, and ipilimumab, for the treatment of metastatic melanoma. Belatacept was discovered by Bristol-Myers Squibb. Ipilimumab is being developed by Bristol-Myers Squibb and Medarex Inc.

10:15 AM BERKELEY, CALIFORNIA It's morning on the West Coast, and Diana Mansfield—running a natural history business selling skeletons and insects—appears healthy and energetic. But 15 years ago, she was diagnosed with incurable kidney disease. “I felt like my life was over,” Mansfield, now age 50, recalls. “I thought, ‘Maybe I’ll die.’” She underwent a kidney transplant in March 2001 and at the same time was invited to participate in a clinical trial at the University of California, San Francisco, of belatacept, an investigational biologic compound from Bristol-Myers Squibb to prevent solid organ transplant rejection. “Now, for the first time in years,” Mansfield says, “I have hope for the future.”





Oncology

Legacy and leadership

Bristol-Myers Squibb provided its first anti-cancer medication for patients more than four decades ago. That medicine, *Cytoxan* (cyclophosphamide), is still being prescribed today. Since then, Bristol-Myers Squibb has become a world leader in cancer therapies. *TAXOL* (paclitaxel), *Paraplatin* (carboplatin) and—most recently—*Erbitux* (cetuximab) have become important weapons in our arsenal of treatments for patients with cancer.

Today, the company is applying its vast store of knowledge and expertise to the discovery and development of the next generation of cancer treatments. With 14 compounds in development, its oncology pipeline is among the most robust of all of Bristol-Myers Squibb's therapeutic areas.

Four oncology compounds are either now in the late stages of clinical development or already awaiting regulatory action. They include:

- **Dasatinib**, an investigational compound discovered by Bristol-Myers Squibb researchers, was submitted to the U.S. Food and Drug Administration (FDA) in December 2005 for the treatment of chronic myelogenous leukemia—a cancer of the bone marrow. Dasatinib is also being studied in other cancers.
- **Ixabepilone**, also discovered by company researchers, is being developed as a potentially first-in-class compound intended to treat taxane-resistant breast cancer and is under investigation for treatment of other solid tumors.
- **Ipilimumab**, a biologic compound, is being developed in collaboration with Medarex Inc. as an immunotherapy for the potential treatment of metastatic melanoma.
- **Vinflunine**, an investigational chemotherapeutic agent licensed from Pierre Fabre Médicament, is in development for bladder, non-small cell lung and breast cancers.

"We are potentially on the verge of unprecedented advances in oncology," says Renzo Canetta, M.D., vice president of Oncology Global Clinical Research. "We are working across a number of areas—in traditional cytotoxics, which we believe will remain the backbone of chemotherapy for the foreseeable future, as well as in biologics and other novel and targeted therapies. This is a very exciting time."

10:45 AM SÃO PAULO, BRAZIL Twice a year for six years, 53-year-old Eduardo Marafanti had his blood tested. He sought to make certain that his chronic myelogenous leukemia, a cancer for which he was being treated, remained under control. But his test results in February 2005 were anything but routine. His doctors discovered that the count of one type of leukemia cells, called blast cells, had skyrocketed. "They said I had just two weeks to live," says Marafanti. He was offered one alternative: to enroll in a clinical trial for dasatinib, an investigational drug discovered by Bristol-Myers Squibb. "I was the first patient in Brazil to enter this clinical trial," he says. Today, Marafanti appears to be doing well. "I hope my experience in this clinical trial offers hope to other patients all over the world."



11:10 AM BEIJING Yang Lifang, 39, lives with her husband and their 16-year-old son. She enjoys cooking, singing karaoke and shopping. In 2000, she tested positive for hepatitis B virus (HBV). Of more than 170 million HBV-infected people in China, the virus kills a half million annually. And despite medical treatment, Lifang's serum HBV levels continued to rise. "I also began to feel extremely tired," she says. Then her doctor recommended that she enter an investigational clinical trial for *Baraclude*. Since entering the trial in 2003, she says, "My viral levels are undetectable. Now I look forward to the future." *Baraclude* received marketing clearance in China in November 2005.



New Approvals

The pipeline delivers

In just over three years—since 2002—six new Bristol-Myers Squibb medicines, each addressing a critical medical need, have been launched or approved. This was among the best performances in the industry for the period.

“For the past several years, the entire R&D organization has been undergoing a significant transformation, seeking to increase its productivity while developing innovative drugs,” says Brian Daniels, M.D., senior vice president for Global Clinical Development. “Our focus has been on satisfying the unmet medical needs of patients while seeking to maximize safety and efficacy.”

Three new Bristol-Myers Squibb medicines were approved by the FDA in 2005 and early 2006:

- **Baraclude** (entecavir), for chronic hepatitis B virus (HBV) infection, was approved in March 2005. Chronic HBV infection can cause cirrhosis and liver cancer. It is the ninth leading cause of death worldwide.
- **Orencia** (abatacept), a novel biologic for the treatment of rheumatoid arthritis, was approved in December 2005. About 6 million people suffer from rheumatoid arthritis worldwide.
- **EMSAM** (selegiline transdermal system), the first transdermal patch for the treatment of major depressive disorder, was approved in February 2006.

Baraclude and *Orencia* were discovered by Bristol-Myers Squibb scientists. EMSAM was licensed from Somerset Pharmaceuticals Inc. Since November 2002, Bristol-Myers Squibb also launched Abilify (aripiprazole) for schizophrenia, *Reyataz* (atazanavir) for HIV, and Erbitux (cetuximab) for metastatic colorectal cancer.



11:35 AM BROOKLYN, NEW YORK In 1988, at age 35, Mario Gutierrez was diagnosed with rheumatoid arthritis. Excruciating joint pain made it impossible for Gutierrez to do everyday things like playing with his children or exercising with his wife, Silvana. Even getting out of bed was difficult. For years, Gutierrez went from treatment to treatment in search of lasting relief. “But I never gave up hope,” he says. Then, in 2002, Gutierrez learned about a clinical trial of *Orencia* that was being conducted at Weill Medical College of Cornell University Hospital for Special Surgery. Since entering the trial, his condition has improved. “Now, to keep in shape,” he says, “I enjoy cycling daily.”






Life Cycle Management

A pipeline within a product

Approval for marketing of a new medicine does not signify the end of its program of clinical studies. Often, it's just the beginning.

"In effect, many of our medicines represent a pipeline within a product," says David Boyko, M.D., senior vice president, Global Medical Affairs and Life Cycle Management. "Even after a new medicine is approved and launched, we continue an intense clinical development program to find new uses and benefits for patients."

Among the products Bristol-Myers Squibb continues to develop are Plavix (clopidogrel bisulfate), Abilify (aripiprazole), *Reyataz* (atazanavir) and Erbitux (cetuximab). For each, ongoing clinical studies continue to evaluate new uses:

- **Plavix:** Plavix was initially approved in 1997, and clinical data over the years have uncovered additional uses. Plavix is used to reduce the risk of heart attack or stroke in patients who have had a recent heart attack or stroke, and those with peripheral artery disease. Taken with aspirin, Plavix is now also used to reduce these risks in patients with acute coronary syndrome (those hospitalized with chest pain or who have had a certain type of heart attack). Since its approval, Plavix has been prescribed for about 48 million patients.
- **Abilify:** First approved in late 2002 for schizophrenia, which affects about 3 million people in the U.S., Abilify was additionally approved in 2004 to treat acute manic or mixed episodes associated with bipolar disorder, which affects up to 12 million. In 2005, Abilify received another approval for use in the U.S. in maintaining efficacy in patients with manic or mixed episodes associated with bipolar disorder who had been previously stabilized and maintained for at least six weeks.

(continued on page 23)

1:45 AM HAYES, ENGLAND In 1993, Melanie Smith was a successful 23-year-old model, fun-loving and curious. But then, a dark cloud engulfed her life. At first, she felt occasionally depressed. Then she sensed people were watching her, following her. One day she called the police. Smith was hospitalized and diagnosed with schizophrenia. "This illness strips patients of everything," says her mother, Kerina, adding that her formerly adventuresome daughter refused to go anywhere. "Her world shrank." After trying other medications, in February 2005, Smith's doctor prescribed Abilify, which has helped ease the symptoms of schizophrenia. Since then, Smith says, "I feel more like my old self."



Life Cycle Management: A pipeline within a product

- **Reyataz:** Reyataz was launched in the U.S. in 2003 as the first once-a-day protease inhibitor for the treatment of HIV in combination with other antiretrovirals; clinical investigations continue in pediatric trials and in patients new to HIV therapy.
- **Erbix:** Erbix was approved by the FDA in 2004 for the treatment of metastatic colorectal cancer in certain patients; approval for a second use, in squamous cell head and neck cancer, was granted in March 2006. Erbix is the first new treatment for this serious illness in nearly three decades. Studies in other tumor types are also ongoing.

“Bristol-Myers Squibb’s portfolio of products continues to expand,” says Wendy Dixon, Ph.D., chief marketing officer and president, Global Marketing. “As it does, the concept of a pipeline within a product also grows.”



12:05 PM CHARLOTTE, NORTH CAROLINA It's just after noon, and wedding planner William Johnson, 46, is selecting flowers for the next event. In early 2004, Johnson began to experience a series of troubling symptoms. He felt stiff and weak. Then he experienced night sweats, forgetfulness, unexplained rashes and weight loss. After a blood test, his doctor told him he had HIV/AIDS. Johnson entered into a clinical trial for patients new to therapy, in which *Reyataz* is used in combination with other antiretroviral agents. “Now,” he says, “I feel better. I’m so glad I had the opportunity to participate in this clinical trial.”

12:15 PM FREEPORT, ILLINOIS Karen Wachin, 64, is taking time to enjoy her great-grandson, Gabriel. Wachin adores puzzles and mysteries, but the biggest mystery she’s experienced began in late 1999 when she noticed a swelling in her jaw. Her physician treated her for swollen glands, but the swelling didn’t go away. Months later, a biopsy revealed advanced tonsil cancer. “I was devastated,” she says. “I thought of my mother, who died of cancer when I was a baby, and I cried all the way home.” Wachin was invited to participate in a clinical trial at the University of Wisconsin involving *Erbix* in combination with radiation for head and neck cancer. Since then, she appears to have done well. “Today,” she says, “I feel lucky, lucky, lucky.”

1:15 PM LEBANON, NEW JERSEY Bob Wise, 58, exercises daily, and as president and CEO of Hunterdon Healthcare System, he has dedicated his life to ensuring that other people get the medical help they need. But a heart attack in 2002 forced Wise—the father of three girls—to focus on his own health. He began an exercise program, and his doctor prescribed a cholesterol-lowering medication and *Plavix*. “My father died of a heart attack at age 44,” he says. “Now I do everything I can to prevent the same thing from happening to me.”





Mead Johnson Nutritionals

A century of excellence

Mead Johnson Nutritionals is a world leader in nutrition, dedicated to providing infants and children with the best start in life. With more than 70 products marketed in over 60 countries, the company is trusted by millions of parents and health care professionals.

In 2005, Mead Johnson celebrated a historic event—its 100th anniversary. It was founded in 1905 by Edward Mead Johnson, Sr., whose passion was to create products that would help infants lead healthier lives.

Since then, Mead Johnson has grown from the dream of one man into a global company with more than 4,500 employees. Yet today, Mead Johnson remains committed to its founder's original

goals—and to achieving them through innovative science-based nutrition as well as by creating trusting relationships with its customers.

Mead Johnson's centennial year was a banner one for the company, with sales of more than \$2 billion due to strong growth in U.S. and international markets. Mead Johnson's *Enfamil* infant formulas are Bristol-Myers Squibb's third-largest brand.

"Mead Johnson has a remarkable past and a very exciting future," says Mead Johnson president Steve Golsby. "We have a clear vision and focused strategies that position Mead Johnson for sustained growth as we continue developing products to meet the nutritional needs of infants and children the world over."

1:30 PM HOMESTEAD, FLORIDA Up from a midday nap, Dixie Dixon looks ready to go.

But when Dixie was born on December 24, 2004, doctors learned that she had an atrial septal defect—a hole in her heart. "Dixie's pediatrician told me I should try to keep her from crying and getting overworked," says her mother, Ghislaine. That would be a challenge for any mom, but especially for Ghislaine because Dixie had colic. The pediatrician suggested she try Mead Johnson's *Nutramigen LIPIL*, a hypoallergenic infant formula designed to help babies with colic due to cow's milk allergy. She did, and the colic disappeared. Doctors say if the hole in her heart does not close on its own by the time she is two years old, she will need surgery. In the meantime, Ghislaine intends to keep Dixie on *Nutramigen LIPIL*. "Dixie's a very determined little girl," says her mom. "Nothing will stop her."



Our Other Health Care Businesses

Renewing hope, bettering lives

2:05 PM VANCOUVER, BRITISH COLUMBIA

It's afternoon in western Canada as Rob Hill trains to complete a physical feat few others have even contemplated: scaling the highest peak on each of the seven continents. But for Hill, 35, the Seven Summits constitute only the second most grueling challenge he has faced. Ten years ago, ulcerative colitis and Crohn's disease forced Hill to have surgery to remove his colon. "It came to losing my colon or losing my life," he says. Shortly after being fitted with a ConvaTec pouching system that enables him to manage the elimination of waste, Hill began working his way back to his superactive life. So far, he has scaled five of the seven peaks: Europe's Elbrus, Africa's Kilimanjaro, South America's Aconcagua, North America's Denali and, most recently, Antarctica's Vinson. By mid-2008, Hill hopes to have scaled Australia's Carstensz Pyramid and Asia's Everest. "Once, because of my illness, I could barely climb up the stairs," Hill says. "Now I want to show that you can live your life and achieve your goals, small or large, no matter who you are."

ConvaTec A world leader in wound therapeutics and ostomy care products, ConvaTec has helped improve the lives of millions of people worldwide through its passion for customer-driven quality, coupled with a fervor for developing breakthrough products.

With 3,000 employees serving customers in 100 countries, ConvaTec's Wound Therapeutics and Chronic Care businesses are giving people hope to overcome challenges and live active, normal lives. Leading products include *AQUACEL Ag*, an innovative antibacterial wound dressing, and the *Esteem synergy* ostomy system.

"We listen to our customers, and they trust us to develop the life-transforming technologies, reliable products and expert services they need to overcome their challenges and live contented, useful lives," says Gary Restani, president, ConvaTec. "Giving people renewed hope is part of our spirit."

Medical Imaging Bristol-Myers Squibb Medical Imaging is helping physicians enhance cardiovascular patient care with its market-leading products in the U.S., including *Cardiolite* (Kit for the Preparation of Technetium Tc99m Sestamibi for Injection)—a pioneering myocardial perfusion imaging agent—as well as the ultrasound contrast agent *Definity* (Vial for Perflutren Lipid Microsphere Injectable Suspension).

"We are proud to contribute to the realization of the Bristol-Myers Squibb vision by propelling the field of cardiovascular imaging forward for the betterment of patients around the world," says Cory Zwerling, president, Bristol-Myers Squibb Medical Imaging.

2:45 PM MISSION VIEJO, CALIFORNIA Stress testing with *Cardiolite* simultaneously assesses both heart blood flow and heart function in a single, noninvasive test. "These images help me determine whether a patient has had a heart attack or is at risk for one in the future," says Greg Thomas, M.D., M.P.H., at Mission Internal Medical Group, pictured here with technologist Lisa Ryals, C.N.M.T.







3:15 PM BILOXI, MISSISSIPPI Day or night, disasters can strike around the world, turning lives upside down. Pediatrician Jennifer Grayson's practice was no match for Hurricane Katrina. The storm surge swept a shrimp boat—along with its elderly captain and his dog—directly on top of her clinic, crushing it. Although the boat's occupants survived, Grayson lost her office. "She was basically down to one stethoscope," says Stan Treadway, a Mead Johnson medical sales representative, shown here surveying the scene with Grayson. Today, she operates out of a new office in North Biloxi and is again serving her patients as they also rebuild their lives.

4:00 PM BANDACEH, INDONESIA Health care specialists for Northwest Medical Teams International Inc. dispense medicines at an orphanage (below). Following the tsunami, Northwest Medical Teams, a not-for-profit humanitarian aid organization based in Portland, Oregon, deployed volunteer disaster relief teams and created sustainable relief programs throughout Indonesia, Sri Lanka and Thailand. Bristol-Myers Squibb contributed antibiotics and other medicines that were used in that effort. Bristol-Myers Squibb also provided medicines and other products for tsunami victims through Direct Relief International, AmeriCares, Interchurch Medical Assistance, MAP International and Project HOPE.



Joining the Relief

Bristol-Myers Squibb and its employees lend a hand

Less than a year after the devastating tsunami struck South Asia, killing tens of thousands and affecting countless more, Bristol-Myers Squibb, its Foundation and its employees were all called into action once more—this time to respond to a new wave of natural disasters. Hurricane Katrina destroyed entire communities in the U.S. Gulf Coast region. Hurricane Stan struck Central America. And a massive earthquake shook Pakistan.

Following the tsunami in Asia, Bristol-Myers Squibb provided \$1.2 million in direct assistance and \$7 million at wholesale value in donated medicines and other needed products. For Hurricane Katrina, Bristol-Myers Squibb donated \$1.1 million in cash to the American Red Cross in addition to product donations totaling \$2.9 million wholesale through partner agencies. Additionally, Mead Johnson Nutritionals and ConvaTec donated nearly \$1 million in products. In Guatemala, the company donated antibiotics through its partner Project HOPE. And in Pakistan, the company worked closely through its partnerships with international relief agencies, including Direct Relief International, AmeriCares and Interchurch Medical Assistance, donating more than \$3 million wholesale in medicines and nutritional products.

As the company sought to help, so did its employees. Thousands donated their own money—which the company's Foundation also matched. Others decided they had to do something more personal. A clinical site manager based in Colorado, for instance, traveled to Sri Lanka and joined a volunteer squad of relief workers. In Pakistan, employees near the remote earthquake region directly supported the relief efforts. And in the U.S., employees worked around the clock to ensure that Katrina victims enrolled in the company's clinical trials were quickly located so that they could continue to receive treatment. Employees also helped provide needed medicines for those displaced, and they pitched in where possible to help ensure that patients were treated.






SECURE THE FUTURE

Helping children in Africa

Person by person, village by village, country by country, Bristol-Myers Squibb's *SECURE THE FUTURE* program has taken a leadership role in fighting HIV/AIDS in southern and West Africa. This innovative effort, initiated in 1999, has supported more than 200 individual projects and has committed \$150 million to rebuild communities and save lives, especially helping those least able to help themselves.

Many of these efforts have focused on children. Bristol-Myers Squibb is partnering with Baylor College of Medicine to create state-of-the-art, environmentally sensitive Pediatric Centers of Excellence across Africa and elsewhere in the developing world, focused specifically on the growing numbers of children and their families affected by HIV/AIDS. Already, centers have been established in Lesotho, Swaziland and Botswana, and centers in Burkina Faso and Uganda will open in 2007. "This is a small country," says Edith Mohapi, M.D., director of the Lesotho center, "and every family is affected by HIV. Thanks to Bristol-Myers Squibb and Baylor College of Medicine, we now have the tools and the infrastructure to make a real difference."

The unique Baylor/Bristol-Myers Squibb partnership has also created another initiative—the Pediatric AIDS Corps. Over the next five years, the Pediatric AIDS Corps will send 250 physicians from leading pediatric programs in the U.S. to Africa, eventually treating approximately 80,000 children who have HIV/AIDS. "In 2006, we will have 50 Pediatric AIDS Corps doctors on the ground in sub-Saharan Africa," says Mark Kline, M.D., director of the Baylor International Pediatric AIDS Initiative. "They are treating and caring for thousands of children, but they're also training local health care professionals so that these programs will be self-sustaining."

4:45 PM GABORONE, BOTSWANA As hot as it is here in the late afternoon, there are still important things to do. "When I see a sick child, I see someone who can live to do great things," says Kebba Jobarteh, M.D., who is working here at the Baylor Children's Clinical Center of Excellence. Jobarteh, 31, completed his pediatrics residency at Columbia University Medical Center, New York, in June 2005. Now, he is a Pediatric AIDS Corps Bristol-Myers Squibb Fellow. "This is something I've strived for my whole life—helping children in Africa."



Patient Access Compassion for those in need

7:00 PM BUNNELL, FLORIDA Time to prepare supper—something Patrick Annese knows a lot about. One year ago, at age 80, Annese was still going strong, on his feet 40 hours a week working as a chef. But then the pain in his legs became unbearable, and he was forced to quit. A vascular surgeon diagnosed peripheral artery disease, performed a vein bypass and prescribed Plavix (clopidogrel bisulfate). Because of the burden of multiple medicines, Annese's wife, Joyce, wrote Bristol-Myers Squibb for help. Soon, she was contacted by a representative of the company's Patient Assistance Foundation. Today, Annese is receiving Plavix at no cost. "I am so impressed with Bristol-Myers Squibb for what its Patient Assistance Foundation is doing for my husband," says Joyce. "It is so good to know that a company cares for the needs of others."

Bristol-Myers Squibb interprets its mission to extend and enhance human life in broad terms: by focusing on unmet medical need, by developing innovative products and by expanding access to its medicines and other health care products.

In the U.S., the company participates in a number of programs to ensure that those in need and who qualify can obtain its medicines at no cost or at a reduced cost:

- In 2005, the company's Patient Assistance Foundation and the Bristol-Myers Squibb/AmeriCares Oncology/Virology Access program provided, free of charge, about \$623 million in medicines at wholesale value to more than 864,000 patients. For information about either program, call 800-736-0003 or access www.bmspaf.org.
- The Partnership for Prescription Assistance is an industrywide program that provides a simple, one-stop resource for nearly 500 prescription assistance programs. Bristol-Myers Squibb led the initiative for this program. Call 888-4PPA-NOW or visit www.pparx.org.
- Bristol-Myers Squibb participates in Together Rx Access for qualified uninsured people under 65 years of age who are otherwise not eligible for Medicare. Call 800-444-4106 or visit www.togetherrxaccess.com.

Outside the U.S., Bristol-Myers Squibb's Global Access Program offers discount pricing of up to 93 percent off the U.S. prices of certain HIV drugs in developing countries.



FINANCIAL REVIEW

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Management's Discussion and Analysis of Financial Condition and Results of Operations

EXECUTIVE SUMMARY

About the Company

Bristol-Myers Squibb Company (BMS, the Company or Bristol-Myers Squibb) is a worldwide pharmaceutical and related health care products company whose mission is to extend and enhance human life by providing the highest quality pharmaceutical and related health care products. The Company is engaged in the discovery, development, licensing, manufacturing, marketing, distribution and sale of pharmaceuticals and related health care products.

The Company has three reportable segments—Pharmaceuticals, Nutritionals and Other Health Care. The Pharmaceuticals segment is made up of the global pharmaceutical and international consumer medicines business. The Nutritionals segment consists of Mead Johnson Nutritionals (Mead Johnson), primarily an infant formula and children's nutritionals business. The Other Health Care segment consists of the ConvaTec, Medical Imaging and Consumer Medicines (U.S. and Canada) businesses. In the third quarter of 2005, the Company completed the sale of its Consumer Medicines business. The Nutritionals and Other Health Care segments are also collectively known as the Health Care Group. For additional information about these segments, see Note 17 "Segment Information."

Business Environment

The Company conducts its business primarily within the pharmaceutical industry, which is highly competitive and subject to numerous government regulations. Many competitive factors may significantly affect the Company's sales of its products, including product efficacy, safety, price and cost-effectiveness, marketing effectiveness, product labeling, quality control and quality assurance of its manufacturing operations, and research and development of new products. To successfully compete for business in the health care industry, the Company must not only demonstrate its products offer medical benefits, but also cost advantages. Currently, most of the Company's new product introductions compete with other products already on the market in the same therapeutic category. The Company manufactures branded products, which are priced higher than generic products. Generic competition is one of the Company's leading challenges globally.

In the pharmaceutical industry, the majority of an innovative product's commercial value is usually realized during the period that the product has market exclusivity. When a product loses exclusivity, it is no longer protected by a patent and is subject to new competing products in the form of generic brands. Upon exclusivity loss of a product, the Company can lose a major portion of that product's sales in a short period of time.

Both in the U.S. and internationally, the health care industry is subject to various government-imposed regulations that authorize prices or price controls that have and will continue to have an impact on the Company's sales. In the U.S., Congress and some state legislatures have considered a number of proposals and have enacted laws that could effect major changes in the health care system, either nationally or at the state level. Driven in part by budget concerns, Medicaid access and reimbursement restrictions have been implemented in some states and proposed in many others. In addition, in December 2003, the Medicare Prescription Drug Improvement and Modernization Act (MMA) was enacted to provide outpatient prescription drug coverage to senior citizens in the United States. The MMA became effective in January 2006. The Company cannot predict the potential impact that this legislation will have on its business; however it could have a negative impact on the Company's U.S. pharmaceutical business as greater federal involvement and budget constraints may increase the likelihood of pricing pressures or controls in the future. In many markets outside the United States, the Company operates in environments of government-mandated, cost-containment programs, or under other regulatory regimes that can exert downward pressure on pricing. Pricing freedom is limited in the United Kingdom, for instance, by the operation of a profit control plan and in Germany by the operation of a reference price system. Companies also face significant delays in market access for new products and more than two years can elapse before new medicines become available in some national markets.

The growth of Managed Care Organizations (MCOs) in the U.S. has played a large role in the competition that surrounds the health care industry. MCOs seek to reduce health care expenditures for participants by making volume purchases and entering into long-term contracts to negotiate discounts with various pharmaceutical providers. Because of the market potential created by the large pool of participants, marketing prescription drugs to MCOs has become an important part of the Company's strategy. Companies compete for inclusion in a MCO formulary and the Company has generally been successful in having its major products included. The Company believes that developments in the managed care industry, including continued consolidation, have had and will continue to have a generally downward pressure on prices.

Pharmaceutical production processes are complex, highly regulated and vary widely from product to product. Shifting or adding manufacturing capacity can be a lengthy process requiring significant capital expenditures and regulatory approvals. Biologics manufacturing involves more complex processes than those of traditional pharmaceutical operations. As biologics become more important to the Company's product portfolio, the Company may continue to make arrangements with third party manufacturers, and expects to make substantial investments to increase its internal capacity to produce biologics on a commercial scale.

The Company has maintained a competitive position in the market and strives to uphold this position, which is dependent on its success in discovering and developing innovative, cost-effective products that serve unmet medical needs.

The Company and its subsidiaries are the subject of a number of significant pending lawsuits, claims, proceedings and investigations. It is not possible at this time reasonably to assess the final outcome of these investigations or litigations. Management continues to believe, as previously disclosed, that during the next few years, the aggregate impact, beyond current reserves, of these and other legal matters affecting the Company is reasonably likely to be material to the Company's results of operations and cash flows, and may be material to its financial condition and liquidity. For additional discussion of legal matters, see Note 20 "Legal Proceedings and Contingencies."

Strategy

The Company continues to execute its strategy for long term growth and is currently on track to complete its strategic transition in 2006 and to attain a period of sustainable sales and earnings growth starting in 2007. This strategy consists of increasing investments behind growth drivers, focusing the Company's research and development programs on products in the pharmaceutical pipeline in disease areas that address significant unmet medical needs, aligning sales and marketing emphasis on specialists and high value primary care prescribers, and implementing initiatives designed to achieve and maintain a more efficient cost base.

The Company is in the process of transforming its pharmaceutical portfolio in favor of growth drivers and specialty products, which include Plavix, Avapro/Avalide, Abilify, *Reyataz*, Erbitux and *Baraclude*. U.S. net sales of these products accounted for 35% of the Company's worldwide pharmaceutical net sales in 2005, compared to 29% in 2004, while worldwide net sales of these products accounted for 36% of the Company's worldwide net sales in 2005 as compared to 29% in 2004.

In December 2005, the U.S. Food and Drug Administration (FDA) approved *Orencia* (abatacept) and it became commercially available in the U.S. in February 2006. *Orencia* is targeted initially at adult patients with moderate to severe rheumatoid arthritis, who have had an inadequate response to certain currently available treatments. A marketing authorization application (MAA) has also been submitted for the product with the European Medicines Evaluation Agency (EMA). In January 2006, a supplemental Biologics License Application (sBLA) was filed with the FDA for the approval of a third-party manufacturing facility to support increased production capacity for *Orencia*. The sBLA is part of the Company's plan to engage in third-party manufacturing arrangements to meet future commercial demand expected to be generated from the approval and commercialization of a variety of biologics.

Also in December 2005, the Company completed the submission of its New Drug Application (NDA) to the FDA for dasatinib, a kinase inhibitor for the potential treatment of chronic myelogenous leukemia (CML). On March 7, 2006, the NDA was accepted and granted priority review for accelerated approval. In January 2006, the Company submitted an MAA for dasatinib to the EMA. In October 2005, an FDA Advisory Committee recommended EMSAM, a transdermal patch for treatment of adults with major depressive disorder, could be safely administered without dietary modifications at the 6mg/24 hour dose. On February 27, 2006, the FDA approved EMSAM for use without dietary modifications at the lowest dose of 6mg/24 hour.

In keeping with its strategy, the Company invested \$2.7 billion in research and development, representing a 10% growth rate over 2004. Research and development dedicated to pharmaceutical products, including milestone payments for in-licensing and development programs, was \$2.5 billion, or 16.5% of Pharmaceutical sales in 2005 compared to \$2.3 billion, or 14.7% of Pharmaceutical sales in 2004.

Another major aspect of the Company's strategy relates to how it does business, specifically in its marketing and sales approaches. Specialists are playing an even greater role in decisions related to patient treatment and care, particularly in the 10 critical disease areas where the Company is focusing its efforts. The Company has realigned its U.S. and European sales forces with a focus on specialists as well as with those primary care physicians who are involved in treating patients in these disease areas.

As part of its strategy, the Company is re-examining its operating costs to achieve and maintain a more efficient cost base. At the end of 2005, the Company launched an initiative to identify and realize productivity savings. Through this initiative, the Company will re-examine its operating model to focus resources on high value priorities; simplify and streamline business processes, governance and decision making; and build the capabilities to sustain these cost reductions for the long term. The Company's goal is to realize a minimum of \$500 million in productivity savings in 2007, an incremental \$100 million in 2008 and implement lasting changes that will make the Company more productive, efficient and effective.

RESULTS OF OPERATIONS

The following discussion of the Company's results of continuing operations excludes the results related to the Oncology Therapeutics Network (OTN) business, which were previously presented as a separate segment, and has been segregated from continuing operations and reflected as discontinued operations for all periods presented. See "—Discontinued Operations" below.

Dollars in Millions	2005	2004	2003	% Change	
				2005 to 2004	2004 to 2003
Net Sales	\$ 19,207	\$ 19,380	\$ 18,653	(1)%	4%
Earnings from Continuing Operations Before Minority Interest and Income Taxes	\$ 4,516	\$ 4,418	\$ 4,680	2%	(6)%
% of net sales	23.5%	22.8%	25.1%		
Provision for income taxes	\$ 932	\$ 1,519	\$ 1,210	(39)%	26%
Effective tax rate	20.6%	34.4%	25.8%		
Earnings from Continuing Operations	\$ 2,992	\$ 2,378	\$ 3,097	26%	(23)%
% of net sales	15.6%	12.3%	16.6%		

Net Sales

Net sales from continuing operations for 2005 decreased 1% to \$19.2 billion compared to 2004. U.S. net sales in 2005 decreased 1% to \$10.5 billion compared to 2004, while international net sales of \$8.7 billion remained relatively constant in 2005 as compared to 2004, including a 2% favorable foreign exchange impact.

In 2004, net sales from continuing operations increased 4% to \$19.4 billion from \$18.7 billion in 2003. U.S. net sales in 2004 remained relatively constant at \$10.6 billion compared to 2003 and international net sales increased 10% to \$8.8 billion in 2004, including a 8% favorable foreign exchange impact, from \$8.0 billion in 2003.

The composition of the change in sales is as follows:

	Total Change	Analysis of % Change		
		Volume	Price	Foreign Exchange
2005 vs. 2004	(1)%	(2)%	—	1%
2004 vs. 2003	4%	—	—	4%

In general, the Company's business is not seasonal. For information on U.S. pharmaceuticals prescriber demand, reference is made to the table within Business Segments under the Pharmaceuticals section below, which sets forth a comparison of changes in net sales to the estimated total prescription growth (for both retail and mail order customers) for certain of the Company's pharmaceutical products.

The Company operates in three reportable segments—Pharmaceuticals, Nutritionals and Other Health Care. In May 2005, the Company completed the sale of OTN, which was previously presented as a separate segment. As such, the results of operations for OTN are presented as part of the Company's results from discontinued operations in accordance with Statement of Financial Standards (SFAS) No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." Accordingly, OTN results of operations in prior periods have been reclassified to discontinued operations to conform with current year presentations. The percent of the Company's net sales by segment were as follows:

Dollars in Millions	2005	2004	2003	% Change	
				2005 to 2004	2004 to 2003
Pharmaceuticals	\$ 15,254	\$ 15,564	\$ 15,025	(2)%	4%
% of net sales	79%	80%	80%		
Nutritionals	2,205	2,001	2,023	10%	(1)%
% of net sales	12%	10%	11%		
Other Health Care	1,748	1,815	1,605	(4)%	13%
% of net sales	9%	10%	9%		
Total	\$ 19,207	\$ 19,380	\$ 18,653	(1)%	4%

The Company recognizes revenue net of various sales adjustments to arrive at net sales as reported on the Consolidated Statement of Earnings. These adjustments are referred to as gross-to-net sales adjustments and are further described in “Critical Accounting Policies” below. The following table sets forth the reconciliation of the Company’s gross sales to net sales by each significant category of gross-to-net sales adjustments:

	For the Year Ended December 31,		
Dollars in Millions	2005	2004	2003
Gross Sales	\$ 23,003	\$ 23,896	\$ 22,992
Gross-to-Net Sales Adjustments			
Prime Vendor Charge-Backs	(1,090)	(1,319)	(1,228)
Women, Infants and Children (WIC) Rebates	(843)	(846)	(854)
Managed Health Care Rebates and Other Contract Discounts	(514)	(660)	(710)
Medicaid Rebates	(595)	(673)	(523)
Cash Discounts	(271)	(311)	(319)
Sales Returns	(164)	(276)	(348)
Other Adjustments	(319)	(431)	(357)
Total Gross-to-Net Sales Adjustments	(3,796)	(4,516)	(4,339)
Net Sales	\$ 19,207	\$ 19,380	\$ 18,653

The decrease in prime vendor charge-backs and managed health care rebates in 2005 was primarily due to lower relative sales volume in this segment due to product mix. The decrease in sales returns was primarily due to lower returns for certain products including *Tequin*, *Pravachol* and *Sustiva*. The decrease in other adjustments was due to lower sales discounts and government rebates in the international businesses.

In 2004, the increases from 2003 for prime vendor charge-backs and Medicaid rebates were primarily due to a shift in sales to products with higher discounts in prime vendor and Medicaid programs while the decrease in sales returns was primarily attributable to higher sales returns in 2003 resulting from discontinued products and product conversions.

The following table sets forth the activities and ending balances of each significant category of gross-to-net sales adjustments:

Dollars in Millions	Prime Vendor Charge-Backs	Women, Infants and Children (WIC) Rebates	Managed Health Care Rebates and Other Contract Discounts	Medicaid Rebates	Cash Discounts	Sales Returns	Other Adjustments	Total
Balance at December 31, 2003	\$ 101	\$ 208	\$ 249	\$ 233	\$ 30	\$ 268	\$ 124	\$ 1,213
Provision related to sales made in current period	1,314	843	646	618	311	270	463	4,465
Provision related to sales made in prior periods	5	3	14	55	—	6	(32)	51
Returns and payments	(1,314)	(820)	(711)	(534)	(308)	(316)	(385)	(4,388)
Impact of foreign currency translation	—	—	—	—	—	1	6	7
Balance at December 31, 2004	106	234	198	372	33	229	176	1,348
Provision related to sales made in current period	1,096	843	509	558	269	191	351	3,817
Provision related to sales made in prior periods	(6)	—	5	37	2	(27)	(32)	(21)
Returns and payments	(1,089)	(825)	(542)	(641)	(278)	(206)	(364)	(3,945)
Impact of foreign currency translation	—	—	(3)	—	—	(2)	(7)	(12)
Balance at December 31, 2005	\$ 107	\$ 252	\$ 167	\$ 326	\$ 26	\$ 185	\$ 124	\$ 1,187

In 2005, the Company recorded gross-to-net sales adjusting charges and credits related to sales made in prior periods. The significant items included charges of \$37 million for Medicaid rebates primarily as a result of higher than expected Medicaid utilization of various products; credits of \$32 million for other adjustments primarily as a result of lower than expected rebates to foreign governments; and credits of \$27 million for sales returns resulting from lower returns for certain products including *Tequin*, *Avapro/Avalide* and *Plavix*.

In 2004, the Company recorded charges of \$55 million for Medicaid rebates related to sales made in prior periods. These charges include \$34 million for rebate claims from prior years by certain states, primarily in relation to Medicaid utilization of oncology products not previously reported to the Company, and other revisions resulting from the availability of additional information. In addition, the Company recorded \$32 million for other adjustments as a result of lower than expected rebates to foreign governments.

No other significant revisions were made to the estimates for gross-to-net sales adjustments in 2005 and 2004.

Pharmaceuticals

The composition of the change in pharmaceutical sales is as follows:

	Analysis of % Change			
	Total Change	Volume	Price	Foreign Exchange
2005 vs. 2004	(2)%	(3)%	—	1%
2004 vs. 2003	4%	1%	(1)%	4%

In 2005, Worldwide Pharmaceuticals sales decreased 2% to \$15,254 million. U.S. pharmaceutical sales in 2005 decreased 3% to \$8,190 million compared to \$8,446 million in 2004, primarily due to the continued impact of exclusivity losses of *Paraplatin* and the Glucophage franchise and increased competition for *Pravachol*, partially offset by increased sales of growth drivers including Plavix, Abilify, Erbitux and *Reyataz*. In aggregate, estimated wholesaler inventory levels of the Company's key pharmaceutical products sold by the U.S. Pharmaceutical business at the end of 2005 were down from the end of 2004 by approximately three-tenths of a month to approximately two and a half weeks. The decline in inventory levels negatively impacted the sales performance of certain products in 2005.

International pharmaceutical sales in 2005 decreased 1%, including a 1% favorable foreign exchange impact to \$7,064 million, primarily due to increased generic competition for *Pravachol* and TAXOL® (paclitaxel), partially offset by increased sales of newer products including *Reyataz* and Abilify as well as growth of Plavix.

In 2004, Worldwide Pharmaceuticals sales increased 4% to \$15,564 million. U.S. pharmaceutical sales in 2004 remained constant at \$8,446 million compared to \$8,431 million in 2003. U.S. sales were negatively affected by increased competition for *Pravachol* and exclusivity losses of *Paraplatin* and the Glucophage franchise, offset by increased sales of Plavix and newer products, including Abilify, *Reyataz* and Erbitux. International pharmaceutical sales in 2004 increased 8% to \$7,118 million, including a 9% favorable foreign exchange impact, primarily due to generic competition for *Pravachol* and TAXOL® (paclitaxel), partially offset by the launches of Abilify, *Reyataz* and continued growth in Plavix and Avapro/Avalide.

Key pharmaceutical products and their sales, representing 80%, 80% and 78% of total pharmaceutical sales in 2005, 2004 and 2003, respectively, are as follows:

Dollars in Millions	% Change				
	2005	2004	2003	2005 to 2004	2004 to 2003
Cardiovascular					
Plavix	\$ 3,823	\$ 3,327	\$ 2,467	15%	35%
Pravachol	2,256	2,635	2,827	(14)%	(7)%
Avapro/Avalide	982	930	757	6%	23%
Coumadin	212	255	303	(17)%	(16)%
Monopril	208	274	470	(24)%	(42)%
Virology					
Reyataz	696	414	88	68%	**
Sustiva	680	621	544	10%	14%
Zerit	216	272	354	(21)%	(23)%
Videx/Videx EC	174	274	267	(36)%	3%
Baraclude	12	—	—	—	—
Other Infectious Diseases					
Cefzil	259	270	327	(4)%	(17)%
Oncology					
TAXOL® (paclitaxel)	747	991	934	(25)%	6%
Erbitux	413	261	—	58%	—
Paraplatin	157	673	905	(77)%	(26)%
Affective (Psychiatric) Disorders					
Abilify (total revenue)	912	593	283	54%	110%
Metabolics					
Glucophage Franchise	172	336	948	(49)%	(65)%
Other Pharmaceuticals					
Efferalgan	283	274	244	3%	12%

** Change is in excess of 200%

- Sales of *Plavix*, a platelet aggregation inhibitor sold by the Company primarily in the U.S., increased 15%, including a 1% favorable foreign exchange impact, to \$3,823 million in 2005 from 2004, primarily due to prescription growth of approximately 13% in the U.S. market. The rate of growth in 2005 reflects a deceleration in the growth rate of sales, compared to a growth rate of 35%, including a 2% favorable foreign exchange impact in 2004 from 2003, primarily due to prescription growth of 24% in the U.S. in 2004. The Company is seeking to enhance the growth rate through several measures, including an expansion of a related direct-to-consumer (DTC) campaign, and the recently-filed sNDA for the results from the COMMIT and CLARITY trials, although there can be no assurance that those efforts will be successful. Sales in 2004 were \$3,327 million and sales were \$2,467 million in 2003. *Plavix* is a cardiovascular product that was launched from the alliance between the Company and Sanofi-Aventis (Sanofi). Market exclusivity for *Plavix* is expected to expire in 2011 in the U.S. and 2013 in the European Union (EU). Statements on exclusivity are subject to any adverse determination that may occur with respect to the *Plavix* patent litigation. For additional information on the *Plavix* patent litigation, see Note 20 "Legal Proceedings and Contingencies."
- Sales of *Pravachol*, an HMG Co-A reductase inhibitor, decreased 14% to \$2,256 million in 2005 from 2004. U.S. sales decreased 10% to \$1,274 million in 2005, primarily due to lower demand resulting from increased competition and the related reduction in wholesaler inventory levels, partially offset by lower managed health care rebates in 2005. Estimated U.S. prescriptions declined by approximately 17% compared to 2004. International sales decreased 19%, including a 1% favorable foreign exchange impact, to \$982 million, reflecting generic competition in key European markets. In 2004, sales for *Pravachol* decreased 7%, including a 4% favorable foreign exchange impact, to \$2,635 million from \$2,827 million in 2003, primarily due to a decrease in U.S. prescription demand of approximately 10% and exclusivity loss in select European markets, including Germany and the UK. The Company entered into a distribution agreement with Watson Pharmaceuticals (Watson) authorizing Watson to distribute pravastatin sodium tablets in the U.S. Market exclusivity protection for *Pravachol* is expected to expire on April 20, 2006 in the U.S. Market exclusivity in the EU expired in 2004, with the exception of France and Sweden, where expiration will occur in August and March 2006, respectively, and in Italy, where expiration will occur in January 2008.
- Sales of *Avapro/Avalide*, an angiotensin II receptor blocker for the treatment of hypertension, also part of the Sanofi alliance, increased 6%, including a 1% favorable foreign exchange impact, to \$982 million in 2005 from 2004. U.S. sales increased 2% to \$574 million in 2005 compared to 2004, primarily due to increased demand, partially offset by a reduction in wholesaler inventory levels in 2005. Estimated total U.S. prescription demand increased approximately 11% compared to 2004. International sales increased 11%, including a 3% favorable foreign exchange impact, to \$408 million from \$368 million in 2004, primarily due to increased sales in Canada, France and Germany. In 2004, sales increased 23%, including a 5% favorable foreign exchange impact, to \$930 million from \$757 million in 2003, primarily due to increased sales in Europe and strong U.S. prescription growth of approximately 15%. U.S. sales increased 19% to \$562 million in 2004 compared to \$474 million in 2003, while international sales increased 30%, including a 12% favorable foreign exchange impact, to \$368 million from \$283 million in 2003. Market exclusivity for *Avapro/Avalide* (known in the EU as *Aprovel/Karvea*) is expected to expire in 2011 in the U.S. and in 2012 in countries in the EU; *Avapro/Avalide* is not currently marketed in Japan.
- Sales of *Coumadin*, an oral anti-coagulant used predominantly in patients with atrial fibrillation or deep venous thrombosis/pulmonary embolism, decreased 17% to \$212 million in 2005 compared to 2004 sales, due to continued competition. Estimated total U.S. prescription demand decreased approximately 19% compared to 2004. Sales in 2004 decreased 16% to \$255 million from \$303 million in 2003, due to increased generic competition. Market exclusivity for *Coumadin* expired in the U.S. in 1997.
- Sales of *Monopril*, a second generation angiotensin converting enzyme (ACE) inhibitor for the treatment of hypertension, decreased 24%, including a 2% favorable foreign exchange impact, to \$208 million in 2005 due to increased generic competition in key European markets. Sales in 2004 were \$274 million, a decrease of 42%, including a 4% favorable foreign exchange impact, from \$470 million in 2003, due to the impact of market exclusivity loss. Market exclusivity protection for *Monopril* expired in 2003 in the U.S. and has expired or is expected to expire between 2001 and 2008 in countries in the EU. *Monopril* is not currently marketed in Japan.
- Sales of *Reyataz*, a protease inhibitor for the treatment of human immunodeficiency virus (HIV), which was launched in the U.S. in the third quarter of 2003 and in Europe in the second quarter of 2004, increased 68% to \$696 million in 2005, primarily due to increased demand. European sales increased 174% to \$203 million in 2005 from \$74 million in 2004. *Reyataz* has achieved an estimated monthly new prescription share of the U.S. protease inhibitor market of approximately 28%. Sales in 2004 were \$414 million compared to \$88 million in 2003. Market exclusivity for *Reyataz* is expected to expire in 2017 in the U.S., in countries in the EU and Japan.
- Sales of *Sustiva*, a non-nucleoside reverse transcriptase inhibitor for the treatment of HIV, increased 10% to \$680 million in 2005 from 2004, primarily due to estimated total U.S. prescription growth of approximately 5%, higher average selling prices and lower sales returns. In 2004, *Sustiva* sales increased 14%, including a 5% favorable foreign exchange impact, to \$621 million from \$544 million in 2003, primarily due to increased demand in 2004 and higher prices. Market exclusivity protection for *Sustiva* is expected to expire in 2013 in the U.S. and in countries in the EU; the Company does not, but others do, market *Sustiva* in Japan.

- Sales of *Zerit*, an antiretroviral agent used in the treatment of HIV, decreased 21%, including a 1% favorable foreign exchange impact, to \$216 million in 2005, primarily as a result of a decrease in estimated total U.S. prescriptions of approximately 31% compared to 2004. In 2004, *Zerit* sales decreased 23%, including a 4% favorable foreign exchange impact, to \$272 million from \$354 million in 2003, primarily as a result of continued decrease in demand due to potential adverse side effects. Market exclusivity protection for *Zerit* is expected to expire in 2008 in the U.S., between 2007 and 2011 in countries in the EU and in 2008 in Japan.
- Sales of *Videx/Videx EC*, an antiretroviral agent used in the treatment of HIV, decreased 36% to \$174 million in 2005 from 2004, primarily due to generic competition in the U.S., which began in the fourth quarter of 2004. In 2004, *Videx/Videx EC* sales increased 3%, including a 6% favorable foreign exchange impact, to \$274 million in 2004 from \$267 million in 2003 due to increased sales in Europe, partially offset by sale declines in the U.S. The Company has a licensing arrangement with the U.S. Government for *Videx/Videx EC*, which by its terms became non-exclusive in 2001. The U.S. Government's intellectual property protection expires in 2007 in the U.S. (which includes an earned pediatric extension) and in Japan, and between 2006 and 2009 in countries in the EU. The license to the Company is non-exclusive, which has allowed another company to obtain a license from the U.S. Government and receive approval for marketing. With respect to *Videx/Videx EC*, the Company has patents covering the reduced mass formulation of *Videx/Videx EC* that expire in 2012 in the U.S., the EU and Japan. However, these patents apply only to the type of reduced mass formulation specified in the patent. Other reduced mass formulations may exist. There is currently no issued patent covering the *Videx EC* formulation.
- *Baraclude*, the Company's internally developed oral antiviral agent for the treatment of chronic hepatitis B, was approved by the FDA in March 2005, and generated sales of \$12 million primarily in the U.S. since its U.S. launch in April 2005. *Baraclude* received approvals from international authorities including China, Mexico, Brazil, Indonesia and Argentina during the second half of 2005. The Company believes that the primary markets for *Baraclude* will be outside the U.S. The Company has a composition of matter patent that expires in the U.S. in 2010.
- Sales of *Cefzil*, an antibiotic for the treatment of mild to moderately severe bacterial infections, decreased 4%, including a 1% favorable foreign exchange impact, to \$259 million in 2005 from 2004, primarily due to lower demand. In 2004, *Cefzil* sales decreased 17%, including a 2% favorable foreign exchange impact, to \$270 million from \$327 million in 2003, primarily due to decreased demand in the U.S., partially offset by higher international sales. Market exclusivity expired in December 2005 in the U.S. and is expected to expire between 2007 and 2009 in the EU.
- Sales of *TAXOL*® (paclitaxel), an anti-cancer agent sold almost exclusively in the non-U.S. markets, were \$747 million in 2005 compared to \$991 million in 2004. Sales of *TAXOL*® (paclitaxel) decreased 25%, including a 1% favorable foreign exchange impact, primarily as a result of increased generic competition in Europe. Generic competition for *TAXOL*® (paclitaxel) in a majority of the major European markets began in the second quarter of 2004 and increased in the second half of 2004. In 2004, *TAXOL*® (paclitaxel) sales increased 6%, including a 9% favorable foreign exchange impact, to \$991 million from \$934 million in 2003, primarily due to generic competition in Europe. Market exclusivity protection for *TAXOL*® (paclitaxel) expired in 2002 in the U.S., in 2003 in the EU and is expected to expire between 2006 and 2013 in Japan.
- Erbitux, used to treat refractory metastatic colorectal cancer, was approved by the FDA in February 2004. Sales of Erbitux, which is sold almost exclusively in the U.S., increased 58% to \$413 million in 2005 compared to \$261 million in 2004. Erbitux is marketed by the Company under a distribution and copromotion agreement with ImClone Systems Incorporated (ImClone). A patent relating to combination therapy with Erbitux expires in 2017. The Company's right to market Erbitux in North America and Japan expires in September 2018. The Company does not, but others do, market Erbitux in countries in the EU.
- Sales of *Paraplatin*, an anti-cancer agent, decreased 77% to \$157 million in 2005 from 2004 due to generic competition in the U.S. that began in mid-2004 and increased with the entry of multiple generic competitors in the fourth quarter of 2004. U.S. sales of *Paraplatin* decreased 95% to \$28 million in 2005 from 2004. In 2004, *Paraplatin* sales decreased 26%, including a 1% favorable foreign exchange impact, to \$673 million from \$905 million in 2003, primarily due to generic competition in the U.S. Market exclusivity protection for *Paraplatin* expired in October 2004 in the U.S., in 2000 in the EU and in 1998 in Japan.

- Total revenue for Abilify, an antipsychotic agent for the treatment of schizophrenia, acute bipolar mania and bipolar disorder, increased 54% to \$912 million in 2005 from 2004, primarily due to demand growth in the U.S. and the continued growth in Europe, which achieved sales of \$140 million in 2005. Estimated U.S. prescription demand grew approximately 42% compared to 2004, partially offset by a reduction in wholesaler inventory levels in 2005. Sales growth in the future could be impacted by a trend involving an overall decrease in the rate of growth in demand for antipsychotic agents in the U.S. In 2004, total revenue for Abilify was \$593 million, compared to \$283 million in 2003. Total revenue for Abilify primarily consists of alliance revenue representing the Company's 65% share of net sales in copromotion countries with Otsuka Pharmaceutical Co., Ltd. (Otsuka). Otsuka's market exclusivity protection for Abilify is expected to expire in 2014 in the U.S. (including the granted patent term extension). The Company also has the right to copromote Abilify in several European countries (the United Kingdom, France, Germany and Spain) and to act as exclusive distributor for the product in the rest of the EU. Market exclusivity protection for Abilify is expected to expire in 2009 for the EU (and may be extended until 2014 if pending supplemental protection certificates are granted). The Company's contractual right to market Abilify expires in November 2012 in the U.S. and Puerto Rico and, for the countries in the EU where the Company has the exclusive right to market Abilify until June 2014. Statements on exclusivity are subject to any adverse determination that may occur with respect to the Abilify patent reexamination. For additional information on this matter, see Note 20 "Legal Proceedings and Contingencies." For additional information on revenue recognition of Abilify, see Note 2 "Alliances and Investments."
- Sales for the Glucophage franchise decreased 49% to \$172 million in 2005, compared to a 65% decrease to \$336 million in 2004 from \$948 million in 2003. The decrease in sales in both 2005 and 2004 primarily resulted from increased generic competition. Market exclusivity protection expired in March 2000 for Glucophage IR, in October 2003 for Glucophage XR and in January 2004 for Glucovance. The Company does not, but others do, market these products in the EU and Japan.
- Sales of *Efferalgan*, a formulation of acetaminophen for pain relief, increased 3%, including a 1% favorable foreign exchange impact, to \$283 million in 2005, primarily due to increased sales in Italy and Spain as a result of a strong flu season in 2005. In 2004, sales increased 12%, including a 12% favorable foreign exchange impact, to \$274 million from \$244 million in 2003.

The estimated U.S. prescription and U.S. prescription growth data provided above includes information only from the retail and mail order channels and do not reflect information from other channels, such as hospitals, institutions and long-term care, among others. The estimated prescription and prescription growth data are based on National Prescription Audit (NPA) data provided by IMS Health (IMS), a supplier of market research for the pharmaceutical industry, as described below.

In most instances, the basic exclusivity loss date indicated above is the expiration date of the patent that claims the active ingredient of the drug or the method of using the drug for the approved indication. In some instances, the basic exclusivity loss date indicated is the expiration date of the data exclusivity period. In situations where there is only data exclusivity without patent protection, a competitor could seek regulatory approval prior to the expiration of the data exclusivity period by submitting its own clinical trial data to obtain marketing approval. The Company assesses the market exclusivity period for each of its products on a case-by-case basis. The length of market exclusivity for any of the Company's products is difficult to predict with certainty because of the complex interaction between patent and regulatory forms of exclusivity and other factors. There can be no assurance that a particular product will enjoy market exclusivity for the full period of time that the Company currently anticipates. The estimates of market exclusivities reported above are for business planning purposes only and are not intended to reflect the Company's legal opinion regarding the strength or weakness of any particular patent or other legal position.

Estimated End-User Demand

The following tables set forth for each of the Company's top 15 pharmaceutical products sold by the U.S. Pharmaceuticals business (based on 2004 annual net sales), for the years ended December 31, 2005, 2004 and 2003 compared to the same periods in the prior year: (a) changes in reported U.S. net sales for the period; (b) estimated total U.S. prescription growth for the retail and mail order channels and the estimated U.S. therapeutic category share of the applicable product, calculated by the Company based on NPA data provided by IMS; and (c) estimated total U.S. prescription growth for the retail and mail order channels and the estimated U.S. therapeutic category share of the applicable product, calculated by the Company based on Next-Generation Prescription Services (NGPS) data provided by IMS.

	Year Ended December 31, 2005			Month Ended December 31, 2005	
	% Change in U.S. Net Sales ^(a)	% Change in U.S. Total Prescriptions		Estimated TRx Therapeutic Category Share % ^(e)	
		NPA Data ^(b)	NGPS Data ^(c)	NPA Data ^(b)	NGPS Data ^(c)
Abilify (total revenue)	35	42	40	11	11
Avapro/Avalide	2	11	12	15	15
Cefzil	(5)	(10)	(11)	2	2
Coumadin	(20)	(19)	(20)	21	20
Dovonex	(7)	(7)	(8)	3	3
Erbix ^(d)	58	N/A	N/A	N/A	N/A
Glucophage Franchise	(52)	(63)	(62)	2	2
Paraplatin ^(d)	(95)	N/A	N/A	N/A	N/A
Plavix	14	13	13	86	86
Pravachol	(10)	(17)	(16)	7	7
Reyataz	33	39	37	31	31
Sustiva	11	5	8	24	23
Tequin	(17)	(30)	(28)	1	1
Videx/Videx EC	(73)	(65)	(65)	2	2
Zerit	(18)	(31)	(30)	7	6

	Year Ended December 31, 2004			Month Ended December 31, 2004	
	% Change in U.S.	% Change in U.S. Total Prescriptions		Estimated TRx Therapeutic Category Share % ^(e)	
	Net Sales ^(a)	NPA Data ^(b)	NGPS Data ^(c)	NPA Data ^(b)	NGPS Data ^(c)
Abilify (total revenue)	98	103	103	9	9
Avapro/Avalide	19	15	18	15	15
Cefzil	(31)	(30)	(29)	2	2
Coumadin	(18)	(17)	(21)	27	27
Dovonex	11	(7)	(6)	3	3
Erbix ^(d)	—	N/A	N/A	N/A	N/A
Glucophage Franchise	(66)	(60)	(61)	3	3
Paraplatin ^(d)	(30)	N/A	N/A	N/A	N/A
Plavix	36	24	27	85	85
Pravachol	(12)	(10)	(9)	9	9
Reyataz	**	**	**	12	12
Sustiva	9	4	11	24	23
Tequin	(27)	(24)	(23)	2	2
Videx/Videx EC	(3)	(4)	3	9	9
Zerit	(32)	(29)	(27)	9	9

	Year Ended December 31, 2003			Month Ended December 31, 2003	
	% Change in U.S.	% Change in U.S. Total Prescriptions		Estimated TRx Therapeutic Category Share % ^(e)	
	Net Sales ^(a)	NPA Data ^(b)	NGPS Data ^(c)	NPA Data ^(b)	NGPS Data ^(c)
Abilify (total revenue)	**	**	***	6	***
Avapro/Avalide	24	15	***	15	***
Cefzil	14	(4)	***	3	***
Coumadin	1	(15)	***	33	***
Dovonex	—	(5)	***	3	***
Erbix ^(d)	—	N/A	N/A	N/A	N/A
Glucophage Franchise	22	(16)	***	14	***
Paraplatin ^(d)	26	N/A	N/A	N/A	N/A
Plavix	27	29	***	82	***
Pravachol	22	2	***	12	***
Reyataz	—	—	***	3	***
Sustiva	13	17	***	11	***
Tequin	7	(21)	***	2	***
Videx/Videx EC	(11)	3	***	6	***
Zerit	(29)	(25)	***	7	***

(a) Reflects percentage change in net sales in dollar terms, including change in average selling prices and wholesaler buying patterns.

(b) Based on a simple average of the estimated number of prescriptions in the retail and mail order channels as provided by IMS.

(c) Based on a weighted average of the estimated number of prescription units (pills) in each of the retail and mail order channels based on data provided by IMS.

(d) Erbitux and Paraplatin specifically, and parenterally administered oncology products in general, do not have prescription-level data because physicians do not write prescriptions for these products. The Company believes therapeutic category share information provided by third parties for these products may not be reliable and accordingly, none is presented here.

(e) The therapeutic categories are determined by the Company as those products considered to be in direct competition with the Company's own products. The products listed above compete in the following therapeutic categories: Abilify (antipsychotics), Avapro/Avalide (angiotensin receptor blockers), Cefzil (branded oral solid and liquid antibiotics), Coumadin (warfarin), Dovonex (anti-inflammatory-antipsoriasis), Glucophage Franchise (oral antidiabetics), Plavix (antiplatelet agents), Pravachol (HMG CoA reductase inhibitors), Reyataz (protease inhibitors), Sustiva (antiretrovirals - third agents), Tequin (branded oral solid antibiotics), Videx/Videx EC (nucleoside reverse transcriptase inhibitors) and Zerit (nucleoside reverse transcriptase inhibitors).

** In excess of 200%.

*** Data for 2003 are not available, therefore this section is omitted.

The Company has historically reported estimated total U.S. prescription growth and estimated therapeutic category share based on NPA data, which IMS makes available to the public on a subscription basis, and a simple average of the estimated number of prescriptions in the retail and mail order channels. In the third quarter of 2005, the Company began disclosing estimated total U.S. prescription growth and estimated therapeutic category share based on both NPA and NGPS data. NGPS data is collected by IMS under a new, revised methodology and has been released by IMS on a limited basis through a pilot program. IMS has publicly announced it expects to make NGPS data available to the public on a subscription basis in 2007. The Company believes that the NGPS data provided by IMS provides a superior estimate of prescription data for the Company's products in the retail and mail order channels. The Company has calculated the estimated total U.S. prescription growth and estimated therapeutic category share based on NGPS data on a weighted average basis to reflect the fact that mail order prescriptions include a greater volume of product supplied compared with retail prescriptions. The Company believes that calculation of the estimated total U.S. prescription growth and estimated therapeutic category share based on the NGPS data and the weighted average approach with respect to the retail and mail order channels provides a superior estimate of total prescription demand. The Company now uses this methodology for its internal demand forecasts.

The estimated prescription growth data and estimated therapeutic category share provided above only include information from the retail and mail order channels and do not reflect information from other channels, such as hospitals, institutions and long-term care, among others. The data provided by IMS are a product of IMS's own record-keeping processes and are themselves estimates based on sampling procedures, subject to the inherent limitations of estimates based on sampling. In addition, the NGPS data is part of a pilot program that is still being refined by IMS.

The Company continuously seeks to improve the quality of its estimates of prescription growth amounts, therapeutic category share percentages and ultimate patient/consumer demand through review of its methodologies and processes for calculation of these estimates and review and analysis of its own and third parties' data used in such calculations. The Company expects that it will continue to review and refine its methodologies and processes for calculation of these estimates and will continue to review and analyze its own and third parties' data used in such calculations.

The following table sets forth for each of the Company's key pharmaceutical products sold by the Company's International Pharmaceuticals reporting segment, including the top 15 pharmaceutical products sold in the Company's major non-U.S. countries (based on 2004 net sales), and for each of the key products sold by the other reporting segments listed below, the percentage change in the Company's estimated ultimate patient/consumer demand for the month of December 2005 compared to the month of September 2005, the month of September 2005 compared to the month of June 2005, and the month of June 2005 compared to the month of March 2005.

	% Change in Demand on a Constant U.S. Dollar Basis		
	December 2005 vs. September 2005	September 2005 vs. June 2005	June 2005 vs. March 2005
International Pharmaceuticals			
Abilify (total revenue)	19	1	50
Avapro/Avalide	—	(13)	14
Bufferin	24	2	(21)
Capoten	—	(10)	—
Dafalgan	18	(4)	(17)
Efferalgan	(2)	39	(43)
Maxipime	8	(13)	(15)
Monopril	4	(26)	(2)
Paraplatin	(1)	(4)	2
Perfalgan	19	(13)	5
Plavix	1	(1)	2
Pravachol	(4)	(16)	7
Reyataz	2	4	5
Sustiva	(1)	(1)	(7)
TAXOL® (paclitaxel)	(4)	(4)	(17)
Videx/Videx EC	3	(14)	3
Zerit	(6)	(21)	(5)
Nutritionals			
Enfamil	—	1	6
Nutramigen	1	(2)	5
Other Health Care			
ConvaTec			
Ostomy	7	7	—
Wound Therapeutics	4	(3)	14
Medical Imaging			
Cardiolite	(7)	(6)	(5)
Consumer Medicines			
Excedrin	N/A	N/A	(13)

Estimated Inventory Months on Hand in the Distribution Channel

The following table sets forth for each of the Company's top 15 pharmaceutical products sold by the Company's U.S. Pharmaceuticals business (based on 2004 annual net sales), the U.S. Pharmaceuticals net sales of the applicable product for each of the six quarters ended September 30, 2004 through December 31, 2005, and the estimated number of months on hand of the applicable product in the U.S. wholesaler distribution channel as of the end of each of the six quarters.

Dollars in Millions	December 31, 2005		September 30, 2005		June 30, 2005	
	Net Sales	Months on Hand	Net Sales	Months on Hand	Net Sales	Months on Hand
Abilify (total revenue)	\$ 175	0.6	\$ 214	0.9	\$ 200	0.7
Avapro/Avalide	168	0.6	147	0.5	157	0.6
Cefzil	46	0.7	27	0.7	30	0.8
Coumadin	50	0.8	49	0.6	42	0.7
Dovonex	33	0.5	31	0.6	36	0.7
Erbix	121	—	106	—	97	—
Glucophage Franchise	29	0.7	38	0.7	44	0.8
Paraplatin	5	0.9	9	1.1	(1)	0.8
Plavix	906	0.6	833	0.4	823	0.6
Pravachol	366	0.6	297	0.5	353	0.7
Reyataz	110	0.5	105	0.6	98	0.8
Sustiva	102	0.6	101	0.6	97	0.8
Tequin	22	0.9	21	0.9	22	0.8
Videx/Videx EC	7	0.9	7	1.1	5	1.0
Zerit	21	0.8	24	0.8	26	0.8

Dollars in Millions	March 31, 2005		December 31, 2004		September 30, 2004	
	Net Sales	Months on Hand	Net Sales	Months on Hand	Net Sales	Months on Hand
Abilify (total revenue)	\$ 161	0.7	\$ 170	0.9	\$ 152	0.6
Avapro/Avalide	102	0.8	154	0.9	148	0.6
Cefzil	50	0.7	60	1.1	30	0.6
Coumadin	42	1.0	69	1.0	58	0.9
Dovonex	30	0.6	40	0.9	34	0.7
Erbix	87	**	88	0.2	83	0.2
Glucophage Franchise	39	1.0	48	1.1	39	1.0
Paraplatin	15	0.9	(12)	1.2	145	1.2
Plavix	673	0.8	816	0.9	781	0.6
Pravachol	258	0.8	433	1.0	318	0.6
Reyataz	92	0.8	99	0.9	75	0.6
Sustiva	103	0.8	103	0.8	95	0.7
Tequin	38	0.7	39	0.9	31	0.7
Videx/Videx EC	10	1.2	25	0.9	27	0.6
Zerit	26	0.8	31	0.9	34	0.7

** Less than 0.1 months on hand.

At December 31, 2004, the estimated value of *Cefzil* inventory in the U.S. wholesaler distribution channel exceeded one month on hand by approximately \$1.6 million. Prescriptions for *Cefzil*, an antibiotic, are typically higher in the winter months in the U.S. As a result, the Company's U.S. wholesalers built higher inventories of the product in the fourth quarter of 2004 to meet that expected higher demand. At March 31, 2005, the Company had worked down U.S. wholesaler inventory levels of *Cefzil* to less than one month on hand, and remained at less than one month on hand in subsequent quarters.

At December 31, 2004, the estimated value of Glucophage Franchise products inventory (Glucophage XR, Glucophage IR, Glucovance and Metaglip) in the U.S. wholesaler distribution channel exceeded one month on hand by approximately \$1.6 million. As with all products, the months on hand estimate for the Glucophage Franchise products is an average of months on hand for all stock-keeping units (SKUs) of the product group. The increase in months on hand of the Glucophage Franchise products at the end of the fourth quarter of 2004 to above one month on hand resulted primarily from the purchase by wholesalers of certain SKUs. After giving effect to these purchases, the increased months on hand for these SKUs were less than one month on hand. However, when the increased months on hand for these SKUs were averaged with all SKUs for the Glucophage Franchise products, the aggregate estimated months on hand exceeded one month. At March 31, 2005, the estimated value of Glucophage Franchise products inventory in the U.S. wholesaler distribution channel had been worked down to approximately one month on hand, and has been worked down to, and remained at, less than one month on hand in subsequent quarters.

In October 2004, the U.S. pediatric exclusivity period for *Paraplatin* (carboplatin) expired. The resulting entry of multiple generic competitors for *Paraplatin* led to a significant decrease in demand for *Paraplatin*, which in turn led to the months on hand of the product in the U.S. wholesaler distribution channel exceeding one month at September 30, 2004, December 31, 2004 and September 30, 2005. The estimated value of *Paraplatin* inventory in the U.S. wholesaler distribution channel over one month on hand was approximately \$6.6 million at September 30, 2004, \$6.0 million at December 31, 2004 and \$0.7 million at September 30, 2005. During this time, the Company continued to monitor *Paraplatin* sales with the intention of working down wholesaler inventory levels to less than one month on hand, and by December 31, 2005, the Company had worked down U.S. wholesaler inventory levels of *Paraplatin* to less than one month on hand.

At March 31 and September 30, 2005, the estimated value of *Videx/Videx EC* inventory in the U.S. wholesaler distribution channel exceeded one month on hand by approximately \$1.1 million and \$0.2 million, respectively. As a result of generic competition in the U.S. commencing in the fourth quarter of 2004, demand for *Videx/Videx EC* decreased significantly. During this time, the Company continued to monitor *Videx/Videx EC* sales with the intention of working down wholesaler inventory levels to less than one month on hand, and by December 31, 2005, the Company had worked down U.S. wholesaler inventory levels of *Videx/Videx EC* to less than one month on hand.

For all products other than Erbitux, the Company determines the above months on hand estimates by dividing the estimated amount of the product in the U.S. wholesaler distribution channel by the estimated amount of out-movement of the product from the U.S. wholesaler distribution channel over a period of 31 days, all calculated as described below. Factors that may influence the Company's estimates include generic competition, seasonality of products, wholesaler purchases in light of increases in wholesaler list prices, new product launches, new warehouse openings by wholesalers and new customer stockings by wholesalers. In addition, such estimates are calculated using third party data, which represent their own record-keeping processes and as such, may also reflect estimates.

The Company maintains inventory management agreements (IMAs) with most of its U.S. pharmaceutical wholesalers, which account for nearly 100% of total gross sales of U.S. pharmaceutical products. Under the current terms of the IMAs, the Company's three largest wholesaler customers provide the Company with weekly information with respect to inventory levels of product on hand and the amount of out-movement of products. These three wholesalers currently account for over 90% of total gross sales of U.S. pharmaceutical products. The inventory information received from these wholesalers excludes inventory held by intermediaries to whom they sell, such as retailers and hospitals, and excludes goods in transit to such wholesalers. The Company uses the information provided by these three wholesalers as of the Friday closest to quarter end to calculate the amount of inventory on hand for these wholesalers at the applicable quarter end. This amount is then increased by the Company's estimate of goods in transit to these wholesalers as of the applicable Friday, which have not been reflected in the weekly data provided by the wholesalers. Under the Company's revenue recognition policy, sales are recorded when substantially all the risks and rewards of ownership are transferred, which in the U.S. Pharmaceutical business is generally when product is shipped. In such cases, goods in transit to a wholesaler are owned by the applicable wholesaler and, accordingly, are reflected in the calculation of inventories in the wholesaler distribution channel. The Company estimates the amount of goods in transit by using information provided by these wholesalers with respect to their open orders as of the applicable Friday and the Company's records of sales to these wholesalers with respect to such open orders. The Company determines the out-movement of a product from these wholesalers over a period of 31 days by using the most recent four weeks of out-movement of a product as provided by these wholesalers and extrapolating such amount to a 31 day basis. The Company estimates inventory levels on hand and out-movements for its U.S. Pharmaceutical business's wholesaler customers other than the three largest wholesalers for each product based on the assumption that such amounts bear the same relationship to the three largest wholesalers' inventory levels and out-movements for such product as the percentage of aggregate sales for all products to these other wholesalers in the applicable quarter bears to aggregate sales for all products to the Company's three largest wholesalers in such quarter. Finally, the Company considers whether any adjustments are necessary to these extrapolated amounts based on such factors as historical sales of individual products made to such other wholesalers and third-party market research data related to prescription trends and patient demand. In addition, the Company receives inventory information from these other wholesalers on a selective basis for certain key products.

The Company's U.S. pharmaceuticals business, through the IMAs discussed above, has arrangements with substantially all of its direct wholesaler customers that allow the Company to monitor U.S. wholesaler inventory levels and require those wholesalers to maintain inventory levels at approximately one month or less of their demand. In the second and third quarters of 2005, the Company negotiated amendments to its IMAs with its three largest wholesalers. The amendments extended the original agreements through December 31, 2005 and established lower limits than the original agreements for inventory levels of Company pharmaceutical products held by the wholesalers. In December 2005, the Company reached two year IMAs in principle with its three largest U.S. wholesalers, which provide the same lower limits of wholesaler inventory levels as the IMA extensions previously negotiated.

To help maintain the product quality of the Company's biologic oncology product, Erbitux, the product is shipped only to end-users and not to other intermediaries (such as wholesalers) to hold for later sales. During 2004 and through May 2005, one of the Company's wholesalers provided warehousing, packing and shipping services for Erbitux. Such wholesaler held Erbitux inventory on consignment and, under the Company's revenue recognition policy, the Company recognized revenue when such inventory was shipped by the wholesaler to the end-user. The above estimates of months on hand for the three months ended March 31, 2005, were calculated by dividing the inventories of Erbitux held by the wholesaler for its own account as reported by the wholesaler as of the end of the quarter by the Company's net sales for the last calendar month of the quarter. The inventory levels reported by the wholesaler are a product of the wholesaler's own record-keeping process. Upon the divestiture of OTN in May 2005, the Company discontinued the consignment arrangement with the wholesaler and thereafter did not have Erbitux consignment inventory. Following the divestiture, the Company sells Erbitux to intermediaries (such as specialty oncology distributors) and ships Erbitux directly to the end users of the product who are the customers of those intermediaries. The Company recognizes revenue upon such shipment consistent with its revenue recognition policy. Accordingly, subsequent to June 30, 2005, there was no Erbitux inventory held by wholesalers.

As previously disclosed, for the Company's Pharmaceuticals business outside of the United States, Nutritionals and Other Health Care business units around the world, the Company has significantly more direct customers, limited information on direct customer product level inventory and corresponding out-movement information and the reliability of third party demand information, where available, varies widely. Accordingly, the Company relies on a variety of methods to estimate direct customer product level inventory and to calculate months on hand for these business units.

The following table, which was posted on the Company's website and furnished on Form 8-K, sets forth for each of the Company's key products sold by the reporting segments listed below, the net sales of the applicable product for each of the four quarters ended March 31, 2005 through December 31, 2005, and the estimated number of months on hand of the applicable product in the direct customer distribution channel for the reporting segment as of the end of each of the four quarters. The estimates of months on hand for key products described below for the International Pharmaceuticals reporting segment are based on data collected for all of the Company's significant business units outside of the United States. Also described further below is information on non-key product(s) where the amount of inventory on hand at direct customers is more than approximately one month and the impact is not de minimis. For the other reporting segments, estimates are based on data collected for the United States and all significant business units outside of the United States.

Dollars in Millions	December 31, 2005		September 30, 2005	
	Net Sales	Months on Hand	Net Sales	Months on Hand
International Pharmaceuticals				
Abilify (total revenue)	\$ 49	0.6	\$ 46	0.8
Avapro/Avalide	109	0.6	104	0.5
Bufferin	36	0.7	31	0.6
Capoten	38	0.8	38	0.9
Dafalgan	34	1.2	34	1.3
Efferalgan	74	1.0	66	1.1
Maxipime	48	0.8	40	0.7
Monopril	43	0.9	48	1.0
Paraplatin	33	0.8	33	0.6
Perfalgan	43	0.6	38	0.7
Plavix	155	0.6	147	0.6
Pravachol	218	0.8	230	0.8
Reyataz	78	0.6	71	0.9
Sustiva	68	0.6	69	0.6
TAXOL® (paclitaxel)	176	0.8	171	0.5
Videx/Videx EC	34	0.9	34	0.9
Zerit	26	0.7	27	0.7
Nutritionals				
Enfamil	277	1.0	230	0.9
Nutramigen	48	1.1	44	1.1
Other Health Care				
ConvaTec				
Ostomy	145	1.0	139	0.9
Wound Therapeutics	112	0.9	104	0.8
Medical Imaging				
Cardiolite	100	1.0	106	0.8
Consumer Medicines				
Excedrin	N/A	N/A	29	N/A

Dollars in Millions	June 30, 2005		March 31, 2005	
	Net Sales	Months on Hand	Net Sales	Months on Hand
International Pharmaceuticals				
Abilify (total revenue)	\$ 40	0.6	\$ 27	0.6
Avapro/Avalide	101	0.4	94	0.4
Bufferin	32	1.0	26	0.5
Capoten	42	0.8	42	0.8
Dafalgan	33	0.8	40	1.3
Efferalgan	55	0.5	88	0.9
Maxipime	52	0.8	46	0.7
Monopril	52	0.7	56	0.6
Paraplatin	34	0.6	29	0.6
Perfalgan	42	0.6	42	0.5
Plavix	145	0.5	141	0.7
Pravachol	272	0.7	262	0.7
Reyataz	85	0.8	57	0.6
Sustiva	70	0.6	70	0.5
TAXOL® (paclitaxel)	182	0.5	201	0.5
Videx/Videx EC	38	0.9	39	0.8
Zerit	33	0.6	33	0.6
Nutritionals				
Enfamil	250	0.9	235	0.9
Nutramigen	47	1.0	44	1.0
Other Health Care				
ConvaTec				
Ostomy	139	0.9	127	0.9
Wound Therapeutics	103	0.8	97	0.8
Medical Imaging				
Cardiolite	108	0.7	102	0.7
Consumer Medicines				
Excedrin	39	1.5	38	1.6

The above months on hand information represents the Company's estimates of aggregate product level inventory on hand at direct customers divided by the expected demand for the applicable product. Expected demand is the estimated ultimate patient/consumer demand calculated based on estimated end-user consumption or direct customer out-movement data over the most recent 31 day period or other reasonable period. Factors that may affect the Company's estimates include generic competition, seasonality of products, direct customer purchases in light of price increases, new product launches, new warehouse openings by direct customers, new customer stockings by direct customers and expected direct customer purchases for governmental bidding situations.

The Company relies on a variety of methods to calculate months on hand for these reporting segments. Where available, the Company relies on information provided by third parties to determine estimates of aggregate product level inventory on hand at direct customers and expected demand. For the reporting segments listed above, however, the Company has limited information on direct customer product level inventory, end-user consumption and direct customer out-movement data. Further, the quality of third party information, where available, varies widely. In some circumstances, such as the case with new products or seasonal products, such historical end-user consumption or out-movement information may not be available or applicable. In such cases, the Company uses estimated prospective demand. In cases where direct customer product level inventory, ultimate patient/consumer demand or out-movement data do not exist or are otherwise not available, the Company has developed a variety of other methodologies to calculate estimates of such data, including using such factors as historical sales made to direct customers and third party market research data related to prescription trends and end-user demand.

As of December 31, 2005, September 30, 2005 and March 31, 2005, *Dafalgan*, an analgesic product sold principally in Europe, had approximately 1.2, 1.3 and 1.3 months of inventory on hand, respectively, at direct customers. The level of inventory on hand is due primarily to private pharmacists purchasing *Dafalgan* approximately once every eight weeks and the seasonality of the product.

As of September 30, 2005, *Efferalgan*, an analgesic product sold principally in Europe, had approximately 1.1 months of inventory on hand, at direct customers. The level of inventory on hand is due primarily to private pharmacists purchasing *Efferalgan* approximately once every eight weeks and the seasonality of the product.

As of December 31, 2005 and September 30, 2005, *Nutramigen* and *Prosobee*, infant nutritional products sold principally in the United States, had approximately 1.1 months of inventory on hand at direct customers. The level of inventory on hand at the end of December 31, 2005 is due primarily to holiday stocking by retailers and at the end of September 2005 is due primarily to the impact of retailers holding higher levels of inventory in response to Hurricane Katrina. The Company plans to continue to monitor sales of *Nutramigen* and *Prosobee* with the intention of working down wholesaler inventory levels to less than one month on hand.

As of June 30, 2005 and March 31, 2005, Excedrin, an analgesic product sold principally in the U.S., had approximately 1.5 months and 1.6 months, respectively, of inventory on hand at direct customers. The level of inventory on hand is due to the customary practice of direct customers holding within their warehouses and stores one and one-half to two months of product on hand. Inventory on hand and percentage change in demand data as of and for the month of September 30, 2005, respectively, is not available for Excedrin, which was included in the third quarter 2005 sale of the Company's Consumer Medicines business.

The Company continuously seeks to improve the quality of its estimates of months on hand of inventories held by its direct customers including thorough review of its methodologies and processes for calculation of these estimates and review and analysis of its own and third parties' data used in such calculations. The Company expects that it will continue to review and refine its methodologies and processes for calculation of these estimates and will continue to review and analyze its own and third parties' data in such calculations. The Company also has and will continue to take steps to expedite the receipt and processing of data for the non-U.S. Pharmaceuticals business.

HEALTH CARE GROUP

Nutritionals

The composition of the change in Nutritional sales is as follows:

	Analysis of % Change			
	Total Change	Volume	Price	Foreign Exchange
2005 vs. 2004	10%	7%	2%	1%
2004 vs. 2003	(1)%	(7)%	6%	—

Key Nutritional product lines and their sales, representing 95%, 94% and 84% of total Nutritional sales in 2005, 2004 and 2003, respectively, are as follows:

Dollars in Millions	% Change				
	2005	2004	2003	2005 to 2004	2004 to 2003
Infant Formulas	\$ 1,576	\$ 1,405	\$ 1,284	12%	9%
<i>Enfamil</i>	992	859	808	15%	6%
Toddler/Children's Nutritionals	529	468	421	13%	11%

Worldwide Nutritional sales increased 10%, including a 1% favorable foreign exchange impact and a 2% unfavorable impact from the divestiture of the Adult Nutritional business, to \$2,205 million in 2005 from 2004. In 2004, Worldwide Nutritional sales were \$2,001 million, a decrease of 1%, including a 10% unfavorable impact from the divestiture of the Adult Nutritional business, from \$2,023 million in 2003. In the first quarter of 2004, the Company divested its Adult Nutritional business.

International sales increased 12%, including a 2% favorable foreign exchange impact and a 1% unfavorable impact from the divestiture of the Adult Nutritional business, to \$1,135 million in 2005 from 2004, primarily due to increased sales of *Enfamil*, *Enfagrow* and toddler and children's nutritional products. In 2004, international sales increased 11%, including a 4% unfavorable impact from the divestiture of the Adult Nutritional business, to \$1,010 million from \$910 million in 2003, primarily due to the increased sales of infant formula and children's nutritional products.

U.S. sales increased 8%, including a 3% unfavorable impact from the divestiture of the Adult Nutritional business, to \$1,070 million in 2005 from 2004, primarily due to increased sales of *Enfamil*. In 2004, U.S. sales decreased 11%, including a 14% unfavorable impact from the divestiture of the Adult Nutritional business, to \$991 million from \$1,113 million in 2003.

Sales of *Enfamil*, the Company's best-selling infant formula, increased 15%, including a 1% favorable foreign exchange impact, to \$992 million in 2005 from 2004, primarily due to strong sales growth and the launch of *Enfamil Gentlease Lipil* infant formula in August 2005. In 2004, *Enfamil* sales increased 6%, including a 1% favorable foreign exchange impact, to \$859 million from \$808 million in 2003, primarily due to an increase in international sales.

Other Health Care

The Other Health Care segment includes ConvaTec and the Medical Imaging business. The composition of the change in Other Health Care segment sales is as follows:

	Analysis of % Change			
	Total Change	Volume	Price	Foreign Exchange
2005 vs. 2004	(4)%	(4)%	(1)%	1%
2004 vs. 2003	13%	7%	1%	5%

Other Health Care sales by business and their key products for the years ended December 31, were as follows:

Dollars in Millions	2005	2004	2003	% Change	
				2005 to 2004	2004 to 2003
ConvaTec	\$ 992	\$ 954	\$ 843	4%	13%
Ostomy	550	551	512	—	8%
Wound Therapeutics	416	391	319	6%	23%
Medical Imaging	602	589	508	2%	16%
<i>Cardiolite</i>	416	406	324	2%	25%
Consumer Medicines	154	272	254	(43)%	7%

- Worldwide ConvaTec sales increased 4%, including a 1% favorable foreign exchange impact, to \$992 million in 2005 from 2004, primarily due to the increase in worldwide sales of wound therapeutic products. Sales of wound therapeutic products increased 6%, including a 1% favorable foreign exchange impact, to \$416 million in 2005 from \$391 million in 2004, primarily due to increased sales of *AQUACEL*. Ostomy sales remained constant at \$550 million in 2005, including a 1% favorable foreign exchange impact. In 2004, ConvaTec sales increased 13%, including an 8% favorable foreign exchange impact, to \$954 million from \$843 million in 2003, primarily due to a 23% increase in worldwide sales of wound therapeutic products.
- Worldwide Medical Imaging sales increased 2% to \$602 million in 2005 from 2004. Sales of *Cardiolite* (Kit for the Preparation of Technetium Tc99m Sestamibi for Injection) increased 2% to \$416 million in 2005 from \$406 million in 2004, primarily due to increased demand. In 2004, Medical Imaging sales increased 16%, including a 1% favorable foreign exchange impact, to \$589 million from \$508 million, driven by increased sales of *Cardiolite*. This increase was partially due to a change in the timing of revenue recognition as a result of new distribution agreements entered into in January 2004.

Geographic Areas

In general, the Company's products are available in most countries in the world. The largest markets are in the United States, France, Japan, Spain, Canada, Italy, Germany and Mexico. The Company's sales by geographic areas were as follows:

Dollars in Millions	2005	2004	2003	% Change	
				2005 to 2004	2004 to 2003
United States	\$ 10,461	\$ 10,613	\$ 10,656	(1)%	—
% of Total	54%	55%	57%		
Europe, Middle East and Africa	5,136	5,470	4,985	(6)%	10%
% of Total	27%	28%	27%		
Other Western Hemisphere	1,592	1,425	1,333	12%	7%
% of Total	8%	7%	7%		
Pacific	2,018	1,872	1,679	8%	11%
% of Total	11%	10%	9%		
Total	\$ 19,207	\$ 19,380	\$ 18,653	(1)%	4%

Sales in the United States decreased 1% in 2005, as a result of lower sales of *Paraplatin* and the Glucophage franchise due to the continuing impact of earlier exclusivity losses, and *Pravachol*, due to lower demand resulting from increased competition. This decrease in sales was mostly offset by increased sales of growth drivers including Plavix, Abilify, Erbitux and *Reyataz*, and strong sales growth of *Enfamil*. In 2004, sales in the United States remained constant with growth in prescription demand for key brands including Plavix, Avapro/Avalide, and *Sustiva*, and newer products including Abilify, *Reyataz*, and Erbitux, offset by lower sales of other products as a result of exclusivity losses for *Monopril*, *Paraplatin*, and the Glucophage franchise.

Sales in Europe, Middle East and Africa decreased 6%, including a 1% favorable foreign exchange impact, as a result of sales decline of *TAXOL*® (paclitaxel), due to increased generic competition, and *Pravachol*, due to exclusivity loss in select markets, including the UK and the Netherlands. This decrease in sales was partially offset by increased sales in major European markets of *Reyataz* and *Abilify*, which were both launched in Europe in the second quarter of 2004. In 2004, sales increased 10%, including an 11% favorable foreign exchange impact, as a result of sales decline of *Pravachol*, due to exclusivity loss in select markets, including Germany and the UK, and *TAXOL*® (paclitaxel), where generic competition in a majority of the major European markets began in the second quarter of 2004. This decrease in sales was mostly offset by increased sales of *Plavix* in Germany and Spain, *Avapro/Avalide* in Italy and Spain, and *Sustiva* in the majority of the major markets.

Sales in the Other Western Hemisphere countries increased 12%, including a 7% favorable foreign exchange impact, primarily due to increased sales of *Plavix* in Canada and Mexico, *Reyataz* in Brazil and Canada, and *Avapro/Avalide* in Canada. In 2004, sales increased 7%, including a 2% favorable foreign exchange impact, primarily due to increased sales of *Plavix* and *Avapro/Avalide* in Canada.

Sales in the Pacific region increased 8%, as a result of increased sales of *TAXOL*® (paclitaxel) in Japan, and *Enfagrow* and *Enfamil* in China. In 2004, sales increased 11%, including a 5% favorable foreign exchange impact, as a result of increased sales of *TAXOL*® (paclitaxel) and *Paraplatin* in Japan, and *Plavix* and *Avapro/Avalide* in Australia.

Expenses

Dollars in Millions				% Change	
				2005 to 2004	2004 to 2003
Cost of products sold	\$ 5,928	\$ 5,989	\$ 5,406	(1)%	11%
% of net sales	30.9%	30.9%	29.0%		
Marketing, selling and administrative	\$ 5,106	\$ 5,016	\$ 4,620	2%	9%
% of net sales	26.6%	25.9%	24.7%		
Advertising and product promotion	\$ 1,476	\$ 1,411	\$ 1,415	5%	—
% of net sales	7.7%	7.3%	7.6%		
Research and development	\$ 2,746	\$ 2,500	\$ 2,279	10%	10%
% of net sales	14.3%	12.9%	12.2%		
Acquired in-process research and development	\$ —	\$ 63	\$ —	(100)%	—
% of net sales	—	0.3%	—		
Provision for restructuring, net	\$ 32	\$ 104	\$ 26	(69)%	**
% of net sales	0.1%	0.5%	0.1%		
Litigation charges, net	\$ 269	\$ 420	\$ 199	(36)%	111%
% of net sales	1.4%	2.2%	1.1%		
Gain on sale of business	\$ (569)	\$ (320)	\$ —	(78)%	—
% of net sales	(3.0)%	(1.7)%	—		
Equity in net income of affiliates	\$ (334)	\$ (273)	\$ (151)	(22)%	(81)%
% of net sales	(1.7)%	(1.4)%	(0.8)%		
Other expense, net	\$ 37	\$ 52	\$ 179	(29)%	(71)%
% of net sales	0.2%	0.3%	1.0%		
Total Expenses, net	\$ 14,691	\$ 14,962	\$ 13,973	(2)%	7%
% of net sales	76.5%	77.2%	74.9%		

** Change is in excess of 200%

- Cost of products sold, as a percentage of sales, were 30.9% in 2005 and 2004, and 29.0% in 2003. In 2005, the unfavorable impact on gross margins resulting from the change in the U.S. pharmaceutical sales mix was offset by \$76 million of net litigation charges recorded in 2004. In 2004, the increase over 2003 was due to the unfavorable impact of U.S. pharmaceutical sales mix due to the impact of generic competition in the U.S. for the *Glucophage* franchise and *Paraplatin*, and the launch of lower margin *Erbix*, partially offset by sales growth of *Abilify*, *Reyataz* and *Plavix*. Gross margins in 2004 were also negatively impacted by \$76 million of net litigation charges and higher accelerated depreciation charges compared with 2003.
- Marketing, selling and administrative expenses, as a percentage of sales, were 26.6% in 2005, 25.9% in 2004, and 24.7% in 2003. In 2005, marketing, selling and administrative expenses increased 2% to \$5,106 million from 2004, primarily due to higher legal costs and higher pension expenses, reflecting increased amortization of unrecognized net losses as well as change in actuarial assumptions, partially offset by lower sales force expenses resulting from a focus on specialists and high value primary care physicians. Marketing, selling and administrative expenses increased 9% to \$5,016 million in 2004 from \$4,620 million in 2003, primarily due to increased sales and marketing support for newer products, including additional sales representatives supporting *Abilify*. In addition, the increase was also related to costs associated with the compliance with the Sarbanes-Oxley Act of 2002 and unfavorable foreign exchange driven by the strengthening of the euro.

- Advertising and product promotion expenditures increased 5% to \$1,476 million as compared to 2004, primarily due to increased investments in direct-to-consumer marketing campaigns for Plavix and Abilify, increased costs associated with pre-launch activities for *Orencia* and the launch of *Baraclude*, partially offset by lower spending on mature products. In 2004, advertising and promotion expenses remained relatively constant at \$1,411 million as compared to \$1,415 million in 2003, with increased investments in Abilify, *Reyataz* and Plavix offset by lower spending on in-line and non-exclusive products.
- The Company's investment in research and development totaled \$2,746 million in 2005, an increase of 10% over 2004 and an increase in 2004 of 10% over 2003. As a percentage of sales, research and development expenses were 14.3% in 2005 compared with 12.9% in 2004 and 12.2% in 2003. In 2005, the increase in research and development expenses reflects continued investments in late-stage compounds. Research and development costs also included \$72 million of charges primarily related to milestone payments for licensing agreements in 2005, \$58 million of charges consisting primarily of upfront and milestone payments in 2004 and \$102 million of charges related to the upfront payments for licensing agreements in 2003. In 2005, research and development spending dedicated to pharmaceutical products increased to 16.5% of Pharmaceuticals sales compared with 14.7% in 2004 and 14.0% in 2003.
- Acquired in-process research and development of \$63 million in 2004 was related to the purchase of Acordis, a UK-based company that is expected to strengthen the Company's leadership position in wound therapeutics. For additional information on the acquisition, see Note 4 "Acquisitions and Divestitures."
- Restructuring programs have been implemented to downsize, realign and streamline operations in order to increase productivity, reduce operating expenses and to rationalize the Company's manufacturing network, research facilities, and the sales and marketing organizations. Actions under the 2005 restructuring program are expected to be complete by 2006 while actions under the 2004 and 2003 restructuring programs were substantially completed at December 31, 2005. As a result of these actions, the Company expects the future annual benefit to earnings from continuing operations before minority interest and income taxes to be approximately \$77 million, \$186 million and \$64 million for the 2005, 2004 and 2003 programs, respectively. For additional information on restructuring, see Note 3 "Restructuring."
- Litigation charges, net of settlement income, were \$269 million in 2005, compared to \$420 million in 2004 and \$199 million in 2003. The \$269 million charge in 2005 consisted of increases to the reserves of \$590 million for liabilities primarily related to private litigations and governmental investigations and partially offset by insurance recoveries of \$321 million. The \$420 million in 2004 consisted of \$336 million related to private litigation and governmental investigations related to wholesaler inventory issues and accounting matters, \$50 million related to the *Platinol* litigation settlement and \$34 million related to pharmaceutical pricing and sales practices. In 2003, the Company established reserves for liabilities in the total amount of \$250 million, comprised of \$150 million in relation to wholesaler inventory issues and certain other accounting matters, and \$100 million in relation to pharmaceutical pricing and sales and marketing practices. In addition, the Company recorded charges of \$31 million for other litigation matters and recognized income of \$82 million. The \$82 million of income consists primarily of \$30 million of income for patent defense cost reimbursement, \$27 million in litigation settlement income and \$21 million from the settlement of anti-trust litigation involving vitamin manufacturers. For additional information on litigation, see Note 20 "Legal Proceedings and Contingencies."
- The gain on sale of business of \$569 million (\$370 million net of tax) in 2005 was related to the sale of the U.S. and Canadian Consumer Medicines business and related assets. The gain on sale of business of \$320 million (\$198 million net of tax) in 2004 was related to the sale of the Adult Nutritional business. For additional information on these transactions, see Note 4 "Acquisitions and Divestitures."
- Equity in net income of affiliates for 2005 was \$334 million, compared with \$273 million and \$151 million in 2004 and 2003, respectively. Equity in net income of affiliates is principally related to the Company's joint venture with Sanofi and investment in ImClone. In 2005, the \$61 million increase in equity in net income of affiliates from 2004 primarily reflects an increase in net income in the Sanofi joint venture, partially offset by a net loss from the investment in ImClone. The \$122 million increase in 2004 from 2003 primarily reflects an increase in net income in the Sanofi joint venture. For additional information on equity in net income of affiliates, see Note 2 "Alliances and Investments."
- Other expenses, net of income, were \$37 million, \$52 million and \$179 million in 2005, 2004 and 2003, respectively. Other expenses include net interest expense, foreign exchange gains and losses, income from third-party contract manufacturing, royalty income and expense, deferred income and debt retirement costs. The \$15 million decrease in other expenses in 2005 from 2004 was primarily due to deferred income recognized from the termination of the collaborative agreement for muraglitazar, partially offset by debt retirement costs in connection with the repurchase of the \$2.5 billion Notes due 2006 and higher net foreign exchange losses. The favorability in 2004 compared to 2003 was primarily due to higher income from third-party contract manufacturing, lower net interest expense and lower net foreign exchange losses. For additional information, see Note 7 "Other Expense, Net."

During the years ended December 31, 2005, 2004 and 2003, the Company recorded several (income)/expense items that affected the comparability of results of the periods presented herein, which are set forth in the following table. For a discussion of these items, see Note 2 "Alliances and Investments"; Note 3 "Restructuring and Other Items"; Note 4 "Acquisitions and Divestitures"; Note 5 "Discontinued Operations"; and Note 20 "Legal Proceedings and Contingencies."

Year ended December 31, 2005

Dollars in Millions	Cost of products sold	Research and development	Provision for restructuring	Gain on sale of business	Litigation settlement expense / (income)	Other (income) / expense, net	Total
Litigation Matters							
Private litigations and governmental investigations	\$ —	\$ —	\$ —	\$ —	\$ 558	\$ —	\$ 558
Pharmaceutical pricing and sales litigation	—	—	—	—	12	—	12
ERISA liability and other matters	—	—	—	—	20	—	20
Insurance recoveries	—	—	—	—	(321)	—	(321)
	—	—	—	—	269	—	269
Other:							
Gain on sale of equity investment	—	—	—	—	—	(27)	(27)
Loss on sale of fixed assets	—	—	—	—	—	18	18
Accelerated depreciation and asset impairment	96	14	—	—	—	—	110
Gain on sale of Consumer Medicines businesses	—	—	—	(569)	—	—	(569)
Upfront and milestone payments	—	44	—	—	—	—	44
Debt retirement costs	—	—	—	—	—	69	69
Downsizing and streamlining of worldwide operations	1	14	32	—	—	—	47
Termination of muraglitazar agreement	5	—	—	—	—	(143)	(138)
	\$ 102	\$ 72	\$ 32	\$ (569)	\$ 269	\$ (83)	(177)
Income taxes on items above							126
Adjustment to taxes on repatriation of foreign earnings							(135)
Increase to Net Earnings from Continuing Operations							<u>\$ (186)</u>

Year ended December 31, 2004

Dollars in Millions	Cost of products sold	Research and development	Acquired in-process research and development	Gain on sale of business	Provision for restructuring and other items, net	Litigation settlement expense / (income)	Other expense, net	Total
Litigation Matters:								
Private litigation and governmental investigations	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 336	\$ —	\$ 336
Product liability	75	—	—	—	—	—	11	86
Pharmaceutical pricing and sales litigation	—	—	—	—	—	34	—	34
Commercial litigation	26	—	—	—	—	—	—	26
Anti-trust litigation	—	—	—	—	—	50	—	50
Product liability insurance recovery	(25)	—	—	—	—	—	—	(25)
	76	—	—	—	—	420	11	507
Other:								
Gain on sale of Adult Nutritional business	—	—	—	(320)	—	—	—	(320)
Accelerated depreciation	100	3	—	—	—	—	4	107
Downsizing and streamlining of worldwide operations	1	—	—	—	104	—	—	105
Upfront and milestone payments	—	55	—	—	—	—	—	55
Acordis IPR&D write-off	—	—	63	—	—	—	—	63
	\$ 177	\$ 58	\$ 63	\$ (320)	\$ 104	\$ 420	\$ 15	517
Income taxes on items above								(130)
Deferred taxes in anticipation of repatriation of foreign earnings								575
Other tax adjustments								10
Reduction to Net Earnings from Continuing Operations								<u>\$ 972</u>

Year ended December 31, 2003

Dollars in Millions	Cost of products sold	Research and development	Provision for restructuring and other items, net	Litigation settlement expense / (income)	Total
Litigation Matters:					
Private litigation and governmental investigations	\$ —	\$ —	\$ —	\$ 150	\$ 150
Product liability	—	—	—	15	15
Pharmaceutical pricing and sales litigation	—	—	—	100	100
Litigation settlement income	—	—	—	(66)	(66)
	—	—	—	199	199
Other:					
Upfront payments for licensing agreements	—	102	—	—	102
Accelerated depreciation and asset impairment charges	64	—	—	—	64
Termination benefits and other exit costs	—	—	53	—	53
Relocation and retention	3	—	13	—	16
Change in estimates	—	—	(40)	—	(40)
	\$ 67	\$ 102	\$ 26	\$ 199	394
Income taxes on items above					(36)
Reduction to Net Earnings from Continuing Operations					<u>\$ 358</u>

Earnings Before Minority Interest and Income Taxes

Dollars in Millions	Earnings From Continuing Operations Before Minority Interest and Income Taxes			% Change	
	2005	2004	2003	2005 to 2004	2004 to 2003
Pharmaceuticals	\$ 3,698	\$ 4,301	\$ 4,414	(14)%	(3)%
Nutritionals	648	586	542	11%	8%
Other Health Care	492	529	363	(7)%	46%
Total segments	4,838	5,416	5,319	(11)%	2%
Corporate/Other	(322)	(998)	(639)	68%	(56)%
Total	\$ 4,516	\$ 4,418	\$ 4,680	2%	(6)%

In 2005, earnings from continuing operations before minority interest and income taxes increased 2% to \$4,516 million from \$4,418 million in 2004. The increase was primarily a result of growth in the Nutritionals segment and the net impact of items that affected the comparability of results as discussed above, partially offset by lower sales and gross margin of pharmaceutical products, primarily due to exclusivity losses and increased spending on research and development, primarily for late-stage pharmaceutical compounds.

In 2004, earnings from continuing operations before minority interest and income taxes decreased 6% to \$4,418 million from \$4,680 million in 2003. Contributing to the decrease in 2004 were increases in costs of products sold as a result of a change in product mix, products losing exclusivity, increased investment in research and development, and the net impact of items that affected the comparability of results as discussed above, partially offset by growth in the Other Health Care segment and higher international sales.

Pharmaceuticals

Earnings before minority interest and income taxes in 2005 were \$3,698 million. The decrease in 2005 from 2004 was primarily due to lower sales and gross margin, primarily due to exclusivity losses, higher advertising and product promotion investments behind growth drivers and increased spending on research and development. Earnings before minority interest and income taxes of \$4,301 million in 2004 decreased from \$4,414 million in 2003 primarily driven by gross margin erosion due to generic competition and product mix, additional sales representatives supporting Abilify, increased spending on research and development, higher non-clinical grants and litigation settlement income in 2003, partially offset by higher sales.

HEALTH CARE GROUP**Nutritionals**

Earnings before minority interest and income taxes in 2005 were \$648 million. The increase in 2005 from 2004 was primarily due to increased worldwide sales of infant formula products and international sales of toddler and children's nutritional products, partially offset by increased investments in advertising and product promotion, and research and development programs. Earnings before minority interest and income taxes increased to \$586 million in 2004 from \$542 million in 2003, primarily due to increased global infant formula sales, a price increase in the infant formula line, favorable manufacturing variances and tight operating expense management.

Other Health Care

Earnings before minority interest and income taxes in 2005 were \$492 million. The decrease in 2005 from 2004 was primarily due to the sale of the U.S. and Canadian Consumer Medicines business and related assets in the third quarter of 2005 and higher spending on research and development, partially offset by sales growth in the ConvaTec and Medical Imaging businesses. Earnings before minority interest and income taxes in the Other Health Care segment increased to \$529 million in 2004 from \$363 million in 2003, primarily due to sales growth in the ConvaTec and Medical Imaging businesses, in addition to favorable pricing and product mix.

Corporate/Other

Earnings/(loss) before minority interest and income taxes in 2005 were a loss of \$322 million. The decrease in 2005 from 2004 was primarily due to the increase on the gain on the sales of businesses/product lines, deferred income recognized from the termination of the collaborative agreement for muraglitazar and a reduction of litigation charges, net. Earnings/(loss) before minority interest and income taxes increased to \$998 million in 2004 from \$639 million in 2003, primarily due to an increase in litigation charges, net; unfavorable foreign exchange driven by the strengthening of the euro; higher pension expenses, reflecting increased amortization of unrecognized net losses as well as change in actuarial assumptions; an increase in downsizing and streamlining of worldwide operations; and an acquired in-process research and development charge in 2004. These increases were partially offset by the increase on the gain on the sale of businesses/product lines.

Income Taxes

The effective income tax rate on earnings from continuing operations before minority interest and income taxes was 20.6% in 2005 compared with 34.4% in 2004 and 25.8% in 2003. The lower effective tax rate in 2005 is due primarily to a 2004 charge of approximately \$575 million for estimated deferred income taxes related to the repatriation of approximately \$9 billion in special dividends from the Company's non-U.S. subsidiaries pursuant to the American Jobs Creation Act of 2004 (AJCA), a 2004 charge related to the establishment of a valuation allowance against certain charitable contributions, a tax benefit in 2005 associated with the release of certain tax contingency reserves resulting from the settlement of examinations by the Internal Revenue Service (IRS) for the years 1998 through 2001, and a change in estimate in 2005 related to the reduction of the aforementioned 2004 AJCA deferred income tax charge, partially offset by lower estimated foreign tax credits in 2005. The increase in the 2004 effective tax rate over the 2003 effective tax rate was primarily attributable to the aforementioned 2004 AJCA deferred tax charge of \$575 million, the aforementioned establishment of a valuation allowance against certain charitable contributions in 2004, an increase in estimates for contingent tax matters, partially offset by the favorable resolution of certain tax refund claims, increased foreign tax credits, and in 2003, the effect of certain litigation reserves as non-deductible.

In the fourth quarter of 2004, the Company disclosed that it anticipated repatriating approximately \$9 billion in special dividends in 2005 and recorded a \$575 million provision for deferred income taxes pursuant to the AJCA as enacted and other pending matters. The Company repatriated approximately \$6.2 billion from foreign subsidiaries in the first quarter of 2005 and repatriated the remaining balance of approximately \$2.8 billion in the fourth quarter of 2005. The Company expects that approximately all of the \$9 billion repatriated in 2005 will qualify as special dividends subject to finalization of its 2005 U.S. federal income tax return and any related tax examinations by the IRS. The Company has used and expects to continue to use the special dividends in accordance with requirements established by the AJCA and the U.S. Treasury Department. During the second quarter of 2005, the U.S. Treasury Department issued AJCA related guidance clarifying that the "gross-up" for foreign taxes associated with the special dividends also qualifies for the 5.25% tax rate established by the AJCA. As a result of this guidance, the Company reduced the \$575 million provision by recording a benefit of approximately \$135 million in its tax provision for 2005. Except for earnings associated with the special dividends discussed above, U.S. income taxes have not been provided on the balance of unremitted earnings of non-U.S. subsidiaries, since the Company has invested or expects to invest such earnings permanently offshore.

The Company has recorded significant deferred tax assets related to U.S. foreign tax credit carryforwards of approximately \$975 million and U.S. research tax credit carryforwards of approximately \$120 million, which expire in varying amounts beginning in 2012. Realization of the foreign tax credit and research tax credit carryforwards is dependent on generating sufficient domestic-sourced taxable income prior to their expiration. Although realization is not assured, management believes it is more likely than not that these deferred tax assets will be realized. The Company anticipates increasing its level of domestic profitability over time by undertaking actions such as increasing its biologics manufacturing capacity in the U.S. While increasing domestic profitability will likely cause the Company's effective tax rate to increase, it will also further enhance the Company's ability to utilize its foreign tax credit and research tax credit carryforwards. The amount of foreign tax credit and research tax credit carryforwards considered realizable, however, could be reduced in the near term if the outcome of the Plavix litigation in the U.S. is unfavorable, and/or if the timing of generic competition for Plavix were to be accelerated. If such events occur, the Company may need to record significant additional valuation allowances against these deferred tax assets. For additional information on Plavix litigation, see Note 20 "Legal Proceedings and Contingencies."

Discontinued Operations

In May 2005, the Company completed the sale of OTN to One Equity Partners LLC for cash proceeds of \$197 million, including the impact of a preliminary working capital adjustment. The Company recorded a pre-tax gain of \$63 million (\$13 million net of tax) that was presented as a gain on sale of discontinued operations in the consolidated statement of earnings. OTN was previously presented as a separate segment. For further discussions of OTN, see Note 5 "Discontinued Operations."

The following amounts related to the OTN business have been segregated from continuing operations and are reflected as discontinued operations for all periods presented:

Dollars in Millions	Year ended December 31,		
	2005	2004	2003
Net sales	\$1,015	\$ 2,506	\$ 2,241
(Loss)/earnings before income taxes	(8)	15	14
Net (loss)/earnings from discontinued operations	(5)	10	9

Developments

On March 1, 2006, the FDA approved Erbitux for use in the treatment of squamous cell carcinoma of the head and neck. As a result of the FDA approval, the Company will pay a \$250 million milestone payment to ImClone by March 31, 2006.

On February 27, 2006, the FDA approved EMSAM, a transdermal patch for treatment of adults with major depressive disorder, for use without dietary modifications at the lowest dose of 6mg/24 hour.

In January 2006, the FDA accepted for review a supplemental New Drug Application (sNDA) for Plavix for treatment of patients with acute ST-segment elevation myocardial infarction (STEMI). The FDA has designated the filing for priority review. Sanofi-Aventis and the Company have also submitted a filing to the EMEA for a STEMI indication in the European Union.

In January 2006, the Company and Gilead Sciences, Inc. (Gilead) announced they have obtained data supporting bioequivalence of a new formulation of the fixed-dose combination of the Company's *Sustiva* and Gilead's *Trudava* (emtricitabine and tenofovir disoproxil fumarate) with the components that make up the new combination. The new fixed-dose regimen is intended for the treatment of HIV-1 infection in adults. Gilead and the Company anticipate submitting an NDA to the FDA in the second quarter of 2006.

In December 2005, the Company completed the submission to the FDA of the NDA for dasatinib to treat chronic myelogenous leukemia (CML) in chronic, accelerated or blast phases, as well as Philadelphia chromosome-positive (Ph+) acute lymphoblastic leukemia (ALL). The NDA seeks approval of dasatinib, an investigational multi-targeted kinase inhibitor, to treat adult chronic myelogenous leukemia. On March 7, 2006, the NDA was accepted and granted priority review for accelerated approval. In January 2006, the Company also submitted an MAA for dasatinib to the EMEA.

In December 2005, the FDA approved *Orencia* and it became commercially available in the U.S. in February 2006. In January 2006, the Company completed submission of the sBLA to the FDA for the licensure of a third-party manufacturing facility to support increased production capacity for *Orencia*.

In December 2005, Exelixis, Inc., (Exelixis) and the Company entered into a collaboration agreement to discover, develop and commercialize novel therapies targeted against the Liver X Receptor (LXR), a nuclear hormone receptor implicated in a variety of cardiovascular and metabolic disorders. Under the collaboration, the companies will jointly identify drug candidates that are ready for Investigational New Drug Application-enabling studies. The Company will undertake further preclinical development and would be responsible for clinical development, regulatory, manufacturing and sales/marketing activities for such compounds. Terms of the agreement include an upfront payment from the Company of approximately \$18 million to Exelixis and will provide research and development funding of approximately \$10 million per year for an initial period of two years. Exelixis also may receive pre-specified development and regulatory milestones totaling approximately \$140 million per product for up to two products from the collaboration, as well as sales milestones and royalties on sales of products commercialized under the collaboration. The agreement received statutory clearance and became effective on January 31, 2006.

In October 2005, the FDA issued an approvable letter for muraglitazar requesting additional information from ongoing clinical trials to more fully address the cardiovascular safety profile of the product. The Company, while continuing discussions with the FDA, has determined that it will likely have to initiate additional new trials to gain regulatory approval and is considering a range of options, including conducting such additional studies or terminating further developments of muraglitazar. The additional studies could take approximately five years to complete. In December 2005, the Company and Merck terminated their collaboration agreement for muraglitazar with all rights returning to the Company as of December 21, 2005. As a result of the termination of the agreement, the Company recognized \$143 million of deferred income in the fourth quarter of 2005, which was recorded in "Other expense, net." The Company has a composition of matter patent which expires in the United States in 2020.

In the third quarter of 2005, the Company completed the sale of its U.S. and Canadian Consumer Medicines business and related assets (Consumer Medicines) to Novartis AG (Novartis). Under the terms of the agreement, Novartis acquired the trademarks, patents and intellectual property rights of Consumer Medicines for \$661 million in cash, of which \$15 million is attributable to a post-closing supply arrangement between the Company and Novartis. The related assets include the rights to the U.S. Consumer Medicines brands in Latin America, Europe, the Middle East and Africa. As a result of this transaction, the Company recorded a pre-tax gain of \$569 million (\$370 million net of tax) in the third quarter of 2005, subject to certain post-closing adjustments.

In June 2005, the Company completed a manufacturing agreement with Celltrion, Inc. for the manufacture of biologic products being developed by the Company.

In April 2005, all manufacturers of atypical antipsychotics, including the Company, received a request from the FDA to add a boxed warning to their U.S. drug labeling noting an increased risk of death in elderly patients with dementia-related psychosis compared with placebo in patients with dementia-related psychosis. The Company has changed the U.S. drug labeling for Abilify in response to the FDA request. Abilify is not approved for the treatment of elderly patients with dementia-related psychosis.

In March 2005, the FDA approved Abilify tablets and oral solution for maintaining efficacy in patients with bipolar I disorder with a recent manic or mixed episode who had been stabilized and then maintained for at least six weeks. The latest FDA approval is based on the positive results of a trial designed to compare the maintenance of efficacy of Abilify versus placebo, measured by time to relapse.

In March 2005, the Company received approval from the FDA for *Baraclude*, an oral antiviral agent for the treatment of chronic hepatitis B. The drug became available in the U.S. in April 2005. The composition of matter patent covering *Baraclude* expires in the U.S. in October 2010, but may be eligible for statutory patent term extension beyond that date. In the second half of 2005, the Company received approvals for *Baraclude* from international authorities including China, Mexico, Brazil, Indonesia and Argentina.

Financial Position, Liquidity and Capital Resources

Cash, cash equivalents and marketable securities totaled approximately \$5.8 billion at December 31, 2005, compared to \$7.5 billion at December 31, 2004. The Company continues to maintain a sufficient level of working capital, which was approximately \$5.4 billion at December 31, 2005, increasing from \$5.0 billion at December 31, 2004. In 2006 and future periods, the Company expects cash generated by its U.S. operations, together with existing cash and borrowings from the capital markets, to sufficiently cover cash needs for working capital, capital expenditures (which the Company expects to include substantial investments in facilities to increase and maintain the Company's capacity to provide biologics on a commercial scale), milestone payments and dividends paid in the United States. Cash and cash equivalents, marketable securities, the conversion of other working-capital items and borrowings are expected to fund near-term operations.

In the fourth quarter of 2004, the Company disclosed that it anticipated repatriating approximately \$9 billion in special dividends in 2005 and recorded a \$575 million provision for deferred income taxes pursuant to the AJCA as enacted and other pending matters. The Company repatriated approximately \$6.2 billion from foreign subsidiaries in the first quarter of 2005 and repatriated the remaining balance of approximately \$2.8 billion in the fourth quarter of 2005. The Company expects that approximately all of the \$9 billion repatriated in 2005 will qualify as special dividends subject to finalization of its 2005 U.S. federal income tax return and any related tax examinations by the IRS. The Company has used and expects to continue to use the special dividends in accordance with requirements established by the AJCA and the U.S. Treasury Department. During the second quarter of 2005, the U.S. Treasury Department issued AJCA related guidance clarifying that the "gross-up" for foreign taxes associated with the special dividends also qualifies for the 5.25% tax rate established by the AJCA. As a result of this guidance, the Company reduced the \$575 million provision by recording a benefit of approximately \$135 million in its tax provision for 2005. Except for earnings associated with the special dividends discussed above, U.S. income taxes have not been provided on the balance of unremitted earnings of non-U.S. subsidiaries, since the Company has invested or expects to invest such earnings permanently offshore.

Cash and cash equivalents at December 31, 2005 primarily consisted of U.S. dollar denominated bank deposits with an original maturity of three months or less. Marketable securities at December 31, 2005 primarily consisted of U.S. dollar denominated floating rate instruments with an 'AAA/Aaa' credit rating. Due to the nature of these instruments, the Company considers it reasonable to expect that their fair market values will not be significantly impacted by a change in interest rates, and that they can be liquidated for cash at short notice. The average interest yield on cash and cash equivalents was 4.1% and 2.3% at December 31, 2005 and 2004, respectively, while interest yields on marketable securities averaged 4.4% and 2.5%, respectively.

Short-term borrowings at the end of 2005 and 2004 were \$231 million and \$1,883 million, respectively, with the reduction of these borrowings due primarily to the retirement of commercial paper. The Company maintains cash balances and short-term investments in excess of short-term borrowings.

Long-term debt at December 31, 2005 was denominated primarily in U.S. dollars but also included Japanese yen debt of \$166 million. Long-term debt was \$8.4 billion at December 31, 2005 compared to \$8.5 billion at December 31, 2004. In August 2005, a wholly-owned subsidiary of the Company entered into a new \$2.5 billion term loan facility with a syndicate of lenders. Borrowings under this facility are guaranteed by the Company, the subsidiaries of the borrower and by certain European subsidiaries of the Company. This facility contains a five-year tranche of up to \$2.0 billion and a two-year tranche of up to \$500 million. The Company is subject to substantially the same covenants as those included in its December 2004 Revolving Credit facility. The Company is also subject to further restrictions, including certain financial covenants. Prior to borrowing any proceeds against the facility, the Company obtained a waiver from the lenders for a covenant default under this facility due to a one-time intercompany distribution. At December 31, 2005, this facility was fully drawn and the Company was in full compliance with all covenants.

During the second quarter of 2005, the Company repurchased all of its outstanding \$2.5 billion aggregate principal amount 4.75% Notes due 2006, and incurred an aggregate pre-tax loss of approximately \$69 million in connection with the early redemption of the Notes and termination of related interest rate swaps.

In December 2004, the Company replaced its prior \$1 billion revolving credit facilities with a new \$2 billion five year revolving credit facility from a syndicate of lenders, which is extendable on the anniversary date with the consent of the lenders. The availability of the facility is subject to the Company's ability at the time of borrowing to meet certain conditions, including a financial covenant in which net debt to capital cannot exceed 50%. This facility does not contain a material adverse change representation in the Company's business as a condition to borrowing. There were no borrowings outstanding under this revolving credit facility at December 31, 2005 and 2004. The Company has been in compliance with this covenant since the inception of the new facility, and as of December 31, 2005, the Company had a ratio of consolidated net debt to consolidated capital of 14%. Changes in public credit ratings will not affect the availability of the credit facility. The Company also had unused short-term lines of credit with foreign banks of \$198 million and \$158 million at December 31, 2005 and 2004, respectively.

A majority of the Company's debt is fixed rate. The Company, however, has entered into fixed to floating interest rate swaps for \$3.4 billion of its long-term debt. Interest expense, net of interest swap gains, was \$349 million, \$310 million, and \$277 million, in 2005, 2004 and 2003, respectively. The increase in interest expense in 2005 from 2004 was primarily due to higher interest rates; the increase in 2004 over 2003 was primarily due to increased short-term borrowings and higher interest rates.

The Moody's Investors Service (Moody's) long-term and short-term credit ratings for the Company are currently A1 and Prime-1, respectively. After the Company's long-term debt rating being under review for downgrade by Moody's, on February 15, 2006, Moody's affirmed the A1 long-term rating. The Company's Prime-1 short-term rating was not under review. The long-term rating retains a negative outlook. Standard & Poor's (S&P) long-term and short-term credit ratings for the Company are currently A+ and A-1, respectively. S&P's long-term credit rating remains on negative outlook. Fitch Ratings (Fitch) long-term and short-term credit rating for the Company are currently A+ and F1, respectively. In September 2005, Fitch's long-term credit rating on the Company was changed from negative to stable outlook.

The following is a discussion of working capital and cash flow activities:

	December 31,	
Dollars in Millions	2005	2004
Working Capital	\$ 5,393	\$ 4,958

	Year Ended December 31,		
Dollars in Millions	2005	2004	2003
Cash flow provided by/(used in):			
Operating activities	\$ 1,836	\$ 3,176	\$ 3,512
Investing activities	1,191	(1,622)	(2,419)
Financing activities	(3,637)	(463)	(1,031)

- The increase in working capital of \$435 million from 2004 was primarily due to: reduction in income taxes payable resulting from payments related to the repatriation of special dividends under the AJCA; lower unrealized losses from derivatives resulting from the weakening of the euro; lower accrued liability for product liability, rebates and returns partially offset by lower receivables resulting from collection of foreign withholding taxes and lower sales volume; higher reserves for litigation matters; and higher inventories due to increased demand of newer products and existing key brands.
- Net cash provided by operating activities was \$1.8 billion in 2005, \$3.2 billion in 2004 and \$3.5 billion in 2003. The decreases in both 2005 and 2004 are mainly attributable to lower earnings and higher usage of working capital. The significant changes in operating assets and liabilities from 2005 and 2004 are: a \$762 million decrease in income tax payable primarily related to the settlement of examinations by the Internal Revenue Service for the years 1998 through 2001 and benefits arising from the resolution of certain tax contingencies; a \$626 million decrease in accounts payable and accrued expenses primarily due to vendor payments prior to the sale of the OTN business and lower accrued rebates and returns; a \$204 million decrease in litigation settlement payments compared to 2004 and \$307 million of insurance recoveries in 2005; a \$237 million increase in inventories due to the growth of newer products and in anticipation of new product launches; a \$231 million decrease in other liabilities primarily due to milestone receipts for the muraglitazar compound in 2004; and a \$1,095 million decrease in receivables primarily due to lower sales volume and foreign withholding taxes. The significant changes in operating assets and liabilities between 2004 and 2003 are: a \$350 million decrease in deferred revenue due to the workdown of consignment inventory in 2003; a \$260 million increase in inventory primarily due to the introduction of new products including *Reyataz* and *Erbix*, higher demand for key brands including *Plavix*, *Avapro/Avalide* and *Sustiva* and a \$146 million decrease in accounts payable and accrued expenses including advertising and promotion, deferred revenue for *Abilify* and milestone payments.

- Net cash provided by investing activities was \$1.2 billion in 2005 compared to net cash used of \$1.6 billion in 2004 and \$2.4 billion in 2003. The \$2,813 million increase in 2005 is attributable to the sale of marketable securities in 2005, proceeds from sale of the Consumer Medicines business for \$646 million in 2005 and a one time \$250 million milestone payment to ImClone in 2004. The decrease in net cash used in investing activities in 2004 is mainly attributable to lower purchases in marketable securities, \$364 million cash proceeds from the sale of the Company's Adult Nutritional business and \$261 million of lower capital spending, partially offset by a milestone payment of \$250 million to ImClone, a \$150 million payment for the Acordis acquisition and increased purchases of trademarks, patents and licenses.
- Net cash used in financing activities was \$3.6 billion in 2005, \$0.5 billion in 2004 and \$1.0 billion in 2003. The \$3,174 million increase in 2005 was mainly attributable to the retirement of commercial paper, and the repurchase of all of the Company's outstanding \$2.5 billion aggregate principal amount 4.75% Notes due 2006, partially offset by \$2.5 billion borrowings against its new term loan facility. The decrease in 2004 from 2003 was mainly attributable to an increase in short-term borrowings in 2004 partially offset by the proceeds received from the issuance of convertible debt in 2003.

Cash provided from operations and borrowings were primarily used over the past three years to pay dividends of approximately \$6.5 billion. The Company has also invested approximately \$2.4 billion over the past three years in capital expansion to improve plant efficiency and maintain superior research facilities.

Over the past three years, the Company did not repurchase any of its common stock. The total shares acquired since the share repurchase program's inception is 372 million shares. The share repurchase program authorizes the Company to purchase common stock from time to time in the open market or through private transactions as market conditions permit. This program is intended to reduce the increase in shares outstanding from option exercises and to obtain shares for general corporate purposes.

Dividends declared per common share were \$1.12 for each of 2005, 2004 and 2003. In December 2005, the Company declared a quarterly dividend of \$.28 per common share and indicated a dividend for the full year 2006 of \$1.12 per share. Dividend decisions are made on a quarterly basis by the Company's Board of Directors.

The Company's financial condition and liquidity could be affected by obligations to make milestone or other one-time payments and by the outcome of pending litigations and investigations, including the challenge to the Plavix patent. For more information, see Note 2 "Alliances and Investments" and Note 20 "Legal Proceedings and Contingencies."

Contractual Obligations

Payments due by period for the Company's contractual obligations at December 31, 2005, are as follows:

Dollars in Millions	Obligations Expiring by Period						
	Total	2006	2007	2008	2009	2010	Later Years
Short-term borrowings	\$ 231	\$ 231	\$ —	\$ —	\$ —	\$ —	\$ —
Long-term debt ⁽¹⁾	8,364	—	504	1,715	3	2,030	4,112
Operating leases	475	129	105	81	58	34	68
Purchase obligations	2,035	486	368	404	389	275	113
Stand-by letters of credit/performance guarantees	74	32	40	—	—	—	2
Pension and other liabilities	1,259	251	219	205	195	187	202
Total	\$ 12,438	\$ 1,129	\$ 1,236	\$ 2,405	\$ 645	\$ 2,526	\$ 4,497

(1) 2006 long-term debt obligations are included in short-term borrowings on the Company's consolidated balance sheet at December 31, 2005 and all balances approximate the outstanding nominal long-term debt values. The contractual obligations table above excludes interest payment obligations. The Company's convertible debenture is included as due for payment in 2008, as it contains a 2008 put and call feature.

In addition to the above, the Company has committed to make potential future "milestone" payments to third-parties as part of in-licensing and development programs. Payments under these agreements generally become due and payable only upon achievement of certain developmental, regulatory and/or commercial milestones. Because the achievement of these milestones is neither probable nor reasonably estimable, such contingencies have not been recorded on the Company's consolidated balance sheet.

For a discussion of contractual obligations, see Note 14 "Short-Term Borrowings and Long-Term Debt"; Note 16 "Financial Instruments"; Note 18 "Leases"; and Note 19 "Pension and Other Postretirement Benefit Plans."

SEC Consent Order and Deferred Prosecution Agreement

As previously disclosed, on August 4, 2004, the Company entered into a final settlement with the SEC, concluding an investigation concerning certain wholesaler inventory and accounting matters. The settlement was reached through a Consent Order (Consent), a copy of which was attached as Exhibit 10 to the Company's quarterly report on Form 10-Q for the period ended September 30, 2004.

Under the terms of the Consent, the Company has agreed, subject to certain defined exceptions, to limit sales of all products sold to its direct customers (including wholesalers, distributors, hospitals, retail outlets, pharmacies and government purchasers) based on expected demand or on amounts that do not exceed approximately one month of inventory on hand, without making a timely public disclosure of any change in practice. The Company has also agreed in the Consent to certain measures that it has implemented including: (a) establishing a formal review and certification process of its annual and quarterly reports filed with the SEC; (b) establishing a business risk and disclosure group; (c) retaining an outside consultant to comprehensively study and help re-engineer the Company's accounting and financial reporting processes; (d) publicly disclosing any sales incentives offered to direct customers for the purpose of inducing them to purchase products in excess of expected demand; and (e) ensuring that the Company's budget process gives appropriate weight to inputs that come from the bottom to the top, and not just those that come from the top to the bottom, and adequately documenting that process.

Further, the Company agreed in the Consent to retain an "Independent Adviser" through the date that the Company's Form 10-K for the year ended 2005 is filed with the SEC. The Independent Adviser continues to serve as the Independent Monitor under the Deferred Prosecution Agreement (DPA) discussed below. The Consent defines certain powers and responsibilities of the Independent Adviser. The Consent includes a process for the Independent Adviser to make recommendations regarding the Company's compliance with applicable federal securities laws and corporate obligations. The Company has agreed in the Consent to adopt the Independent Adviser's recommendations regarding compliance with applicable federal securities laws and corporate obligations.

As previously disclosed, on June 15, 2005, the Company entered into a DPA with the United States Attorney's Office (USAO) for the District of New Jersey resolving the investigation by the USAO of the Company relating to wholesaler inventory and various accounting matters covered by the Company's settlement with the SEC. Pursuant to the DPA, the USAO filed a criminal complaint against the Company alleging conspiracy to commit securities fraud, but will defer prosecution of the Company and dismiss the complaint after two years if the Company satisfies all of the requirements of the DPA. A copy of the DPA was filed as Exhibit 99.2 to a Form 8-K filed by the Company on June 16, 2005 and is incorporated by reference hereto as Exhibit 10w.

Under the DPA, among other things, the Company has agreed to include in its Forms 10-Q and 10-K filed with the SEC and in its annual report to shareholders the following information: (a) estimated wholesaler/direct customer inventory levels of the top fifteen (15) products sold by the U.S. Pharmaceuticals business; (b) for major non-U.S. countries, estimated aggregate wholesaler/direct-customer inventory levels of the top fifteen (15) pharmaceutical products sold in such countries taken as a whole measured by aggregate annual sales in such countries; (c) arrangements with and policies concerning wholesaler/direct customers and other distributors for these products, including efforts by the Company to control and monitor wholesaler/distributor inventory levels; and (d) data concerning prescriptions or other measures of end-user demand for these products. Pursuant to the DPA, the Company also will include in such filings and reports information on acquisition, divestiture, and restructuring reserve policies and activity, and rebate accrual policies and activity.

The Company also agreed to implement remedial measures already undertaken or mandated in the Consent and in the settlements of the derivative litigation and the federal securities class action relating to wholesaler inventory and various accounting matters. In addition, the Company agreed to undertake additional remedial actions, corporate reforms and other actions, including: (a) appointing an additional non-executive Director acceptable to the USAO; (b) establishing and maintaining a training and education program on topics that include corporate citizenship and financial reporting obligations; (c) making an additional \$300 million payment into the shareholder compensation fund established in connection with the Consent; (d) not engaging in or attempting to engage in any criminal conduct as that term is defined in the DPA; (e) continuing to cooperate with the USAO, including with respect to the ongoing investigation regarding individual current and former employees of the Company; and (f) retaining an Independent Monitor. Also as part of the DPA, the Board of Directors separated the roles of Chairman and Chief Executive Officer of the Company and on June 15, 2005, elected a Non-Executive Chairman.

The Independent Monitor, who also serves as the Independent Adviser pursuant to the Consent, has defined powers and responsibilities under the DPA, including the responsibility to oversee at least through April 2007, the Company's compliance with all of the terms of the DPA, the Consent and the settlements of the derivative action and the federal securities class action. The Monitor has the authority to require the Company to take any steps he believes necessary to comply with the terms of the DPA and the Company is required to adopt all recommendations made by the Monitor, unless the Company objects to the recommendation and the USAO agrees that adoption of the recommendation should not be required. In addition, the Independent Monitor will report to the USAO, on at least a quarterly basis, as to the Company's compliance with the DPA and the implementation and effectiveness of the internal controls, financial reporting, disclosure processes and related compliance functions of the Company.

The Company has established a company-wide policy to limit its sales to direct customers for the purpose of complying with the Consent. This policy includes the adoption of various procedures to monitor and limit sales to direct customers in accordance with the terms of the Consent. These procedures include a governance process to escalate to appropriate management levels potential questions or concerns regarding compliance with the policy and timely resolution of such questions or concerns. In addition, compliance with the policy will be monitored on a regular basis.

The Company maintains inventory management agreements (IMAs) with most of its U.S. pharmaceutical wholesalers that account for nearly 100% of total gross sales of U.S. pharmaceutical products. Under the current terms of the IMAs, the Company's three largest wholesaler customers provide the Company with weekly information with respect to months on hand product level inventories and the amount of out-movement of products. These three wholesalers currently account for over 90% of total gross sales of U.S. pharmaceutical products. The inventory information received from these wholesalers, together with the Company's internal information, is used to estimate months on hand product level inventories at these wholesalers. The Company estimates months on hand product inventory levels for its U.S. Pharmaceutical business's wholesaler customers other than the three largest wholesalers by extrapolating from the months on hand calculated for three largest wholesalers. The Company considers whether any adjustments are necessary to these extrapolated amounts based on such factors as historical sales of individual products made to such other wholesalers and third-party market research data related to prescription trends and patient demand. In contrast, for the Company's Pharmaceutical business outside of the United States, Nutritionals and Other Health Care business units around the world, the Company has significantly more direct customers, limited information on direct customer product level inventory and corresponding out-movement information and the reliability of third party demand information, where available, varies widely. Accordingly, the Company relies on a variety of methods to estimate months on hand product level inventories for these business units.

The Company discloses for each of its top fifteen (15) pharmaceutical products sold by the U.S. Pharmaceutical business (based on 2004 net sales) the amount of net sales and the estimated number of months on hand in the U.S. wholesaler distribution channel as of the end of the immediately preceding quarter and as of the end of the applicable quarter in its quarterly and annual reports on Forms 10-Q and 10-K. The Company discloses corresponding information for the top fifteen (15) pharmaceutical products sold within its major non-U.S. countries, as described above. For all other business units, the Company will continue to disclose on a quarterly basis the key product level inventories. The information required to estimate months on hand product level inventories in the direct customer distribution for the non-U.S. Pharmaceutical businesses is not available prior to the filing of the quarterly report on Form 10-Q for an applicable quarter. Accordingly, the Company discloses this information on its website approximately 60 days after the end of the applicable quarter, and in the Company's Form 10-Q for the following quarter. In addition to the foregoing quarterly disclosure, the Company includes all the foregoing information for all business units for each quarter in its Annual Report on Form 10-K. For non-key products, if the inventory at direct customers exceeds approximately one month on hand, the Company will disclose the estimated months on hand for such product(s), except where the impact on the Company is de minimis.

The Company has enhanced and will continue to enhance its methods to estimate months on hand product inventory levels for the U.S. Pharmaceutical business and for the non-U.S. Pharmaceutical businesses around the world, taking into account the complexities described above. The Company also has taken and will continue to take steps to expedite the receipt and processing of data for the non-U.S. Pharmaceutical businesses.

The Company believes the above-described procedures provide a reasonable basis to ensure compliance with both the Consent Order and the DPA and provides sufficient information to comply with disclosure requirements of both.

Recently Issued Accounting Standards

In May 2005, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 154, *Accounting Changes and Error Corrections*, which replaces Accounting Principles Board (APB) Opinion No. 20, *Accounting Changes* and SFAS No. 3, *Reporting Accounting Changes in Interim Financial Statements*. This pronouncement applies to all voluntary changes in accounting principle and revises the requirements for accounting for and reporting a change in accounting principle. SFAS No. 154 requires retrospective application to prior periods' financial statements of a voluntary change in accounting principle, unless it is impracticable to do so. This pronouncement also requires that a change in the method of depreciation, amortization, or depletion for long-lived, non-financial assets be accounted for as a change in accounting estimate that is effected by a change in accounting principle. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The Statement does not change the transition provisions of any existing accounting pronouncements, including those that are in a transition phase as of the effective date of SFAS No. 154. The adoption of this accounting pronouncement is not expected to have a material effect on the consolidated financial statements.

In March 2005, the FASB issued FASB Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations* (FIN 47). FIN 47 clarifies that an entity must record a liability for a conditional asset retirement obligation if the fair value of the obligation can be reasonably estimated. Asset retirement obligations covered by FIN 47 are those for which an entity has a legal obligation to perform an asset retirement activity, even if the timing and method of settling the obligation are conditional on a future event that may or may not be within the control of the entity. FIN 47 also clarifies when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation. FIN 47 is effective no later than the end of fiscal years ending after December 15, 2005. The adoption of this accounting pronouncement did not have a material effect on the consolidated financial statements.

In December 2004, the FASB issued revised SFAS No. 123 (SFAS No. 123R), *Share-Based Payment*. This standard eliminates the ability to account for share-based compensation transactions using the intrinsic value-based method under APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and requires instead that such transactions be accounted for using a fair-value-based method. In April 2005, the SEC delayed the effective date of SFAS No. 123R to financial statements issued for the first annual period beginning after June 15, 2005. The Company adopted SFAS No. 123R on January 1, 2006 using the prospective transition method. As a result of the provisions in SFAS 123R and Staff Accounting Bulletin (SAB) No. 107, the Company estimates that the compensation charges related to share-based compensation for 2006 to be on a pre-tax basis between \$135 million and \$145 million which includes \$80 million to \$85 million of stock option expense due to the adoption of this standard. On an after tax basis, the compensation charges related to share-based compensation for 2006 are estimated to be between \$85 million and \$91 million and the stock option expense due to the adoption of this standard included in these after tax amounts is \$50 million to \$54 million. However, the assessment of the estimated compensation charges is affected by the Company's stock price as well as a number of complex and subjective variables and the related tax impacts. These variables include, but are not limited to, the volatility of the Company's stock price and employee stock exercise behaviors. See Note 1 "Accounting Policies —Stock Compensation Plans."

In December 2004, the FASB issued final staff position (FSP) No. 109-1, *Application of SFAS No. 109, Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004*. The FSP provides that the deduction on qualified production activities will be treated as a "special deduction" as described in SFAS No. 109, *Accounting for Income Taxes*. Accordingly, the tax effect of this deduction will be reported as a component of the Company's current tax provision and will not have an effect on deferred tax assets and liabilities. The Department of the Treasury recently issued Proposed Tax Regulations with respect to the *Deduction on Qualified Production Activities*. The Company is evaluating the impact of the Proposed Tax Regulations and the FSP on its income tax provision and results of operations. See Note 1 "Accounting Policies—Income Taxes."

In December 2004, the FASB issued SFAS No. 153, *Exchanges of Nonmonetary Assets*. The provisions of this Statement are effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005 and should be applied prospectively. The Statement eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets in paragraph 21(b) of APB Opinion No. 29, *Accounting for Nonmonetary Transactions*, and replaces it with an exception for exchanges that do not have commercial substance. The adoption of this accounting pronouncement did not have a material effect on the consolidated financial statements.

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs – an Amendment of ARB No. 43, Chapter 4*. The standard requires abnormal amounts of idle facility and related expenses to be recognized as current period charges and also requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. SFAS No. 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. The adoption of this accounting pronouncement is not expected to have a material effect on the consolidated financial statements.

In June 2004, the FASB issued FSP-No. 106-2, *Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003* (the Medicare Act). The Medicare Act introduces a prescription drug benefit under Medicare as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. FSP No. 106-2 requires that the effects of the new law be accounted for under SFAS No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*. The Company adopted FSP No. 106-2 in the third quarter of 2004, retroactive to January 1, 2004. There was a reduction in net periodic benefit cost for other benefits of \$8 million for 2004, based on the re-measurement of the accumulated postretirement benefit obligation as of January 1, 2004. The effect of the adoption of FSP No. 106-2 was not material to the Company's consolidated financial statements. See Note 19 "Pension and Other Postretirement Benefit Plans."

In March 2004, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 03-06, *Participating Securities and the Two-Class Method Under FAS 128*, which requires the use of the two-class method of computing earnings per share for those enterprises with participating securities or multiple classes of common stock. The consensus is effective for fiscal periods beginning after March 31, 2004. The adoption of EITF No. 03-06 did not have a material effect on the consolidated financial statements.

In December 2003, the FASB revised Interpretation No. 46, *Consolidation of Variable Interest Entities* (FIN 46). FIN 46 requires a variable interest entity to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity's activities or is entitled to receive a majority of the entity's residual returns or both. FIN 46 also requires disclosures about variable interest entities that a company is not required to consolidate but in which it has a significant variable interest. The consolidation requirements of FIN 46 (as revised) apply immediately to variable interest entities created after January 31, 2003 and to existing entities in the first fiscal year or interim period ending after March 15, 2004. Certain of the disclosure requirements apply to all financial statements issued after January 31, 2003, regardless of when the variable interest entity was established. The adoption of this accounting pronouncement did not have a material effect on the consolidated financial statements.

Critical Accounting Policies

The Company prepares its financial statements in conformity with accounting principles generally accepted in the United States. The preparation of financial statements in conformity with U.S. Generally Accepted Accounting Principles (GAAP) requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities, including disclosure of contingent assets and contingent liabilities, at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. The Company's critical accounting policies are those that are both most important to the Company's financial condition and results of operations and require the most difficult, subjective or complex judgments on the part of management in their application, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Because of the uncertainty of factors surrounding the estimates or judgments used in the preparation of the consolidated financial statements, actual results may vary from these estimates.

The Company believes that the following discussion represents its critical accounting policies. Management and the Company's independent registered public accounting firm have discussed the Company's critical accounting policies with the Audit Committee of the Board of Directors.

Revenue Recognition

The Company recognizes revenue in accordance with SAB No. 101, *Revenue Recognition in Financial Statements*, as amended by SAB No. 104, *Revenue Recognition*. The Company's accounting policy for revenue recognition has a substantial impact on its reported results and relies on certain estimates that require difficult, subjective and complex judgments on the part of management. The Company recognizes revenue when substantially all the risks and rewards of ownership have transferred to the customer, which generally occurs on the date of shipment, with the exceptions described below.

In previous years, certain transactions with the Company's U.S. pharmaceutical wholesalers were accounted for using the consignment model. In the case of sales made to wholesalers (1) as a result of incentives, (2) in excess of the wholesaler's ordinary course of business inventory level, (3) at a time when there was an understanding, agreement, course of dealing or consistent business practice that the Company would extend incentives based on levels of excess inventory in connection with future purchases, and (4) at a time when such incentives would cover substantially all, and vary directly with, the wholesaler's cost of carrying inventory in excess of the wholesaler's ordinary course of business inventory level, substantially all the risks and rewards of ownership do not transfer upon shipment, and accordingly, such sales should be accounted for using the consignment model. The determination of when, if at all, sales to a wholesaler meet the foregoing criteria involves evaluation of a variety of factors and a number of complex judgments. Under the consignment model, the Company does not recognize revenue upon shipment of product. Rather, upon shipment of product the Company invoices the wholesaler, records deferred revenue at gross invoice sales price, and classifies the inventory held by the wholesalers as consignment inventory at the Company's cost of such inventory. The Company recognizes revenue (net of the gross to net sales adjustments discussed below, all of which involve significant estimates and judgments) when the consignment inventory is no longer subject to incentive arrangements, but not later than when such inventory is sold through to the wholesalers' customers, on a first-in first-out (FIFO) basis.

In the case of new products for which the product introduction is not an extension of an existing line of product, where the Company determines that there are not products in a similar therapeutic category, or where the Company determines the new product has dissimilar characteristics with existing products, such that the Company cannot reliably estimate expected returns of the new product, the Company defers recognition of revenue until the right of return no longer exists or until the Company has developed sufficient historical experience to estimate sales returns.

For discussions on revenue recognition, see Note 1 "Accounting Policies—Revenue Recognition and Sales Rebate and Return Accruals."

Gross to Net Sales Adjustments

The Company has the following significant categories of gross to net sales adjustments that impact the Company's three reportable segments: prime vendor charge-backs, WIC rebates, managed health care rebates and other contract discounts, Medicaid rebates, cash discounts, sales returns, and other adjustments, all of which involve significant estimates and judgments and require the Company to use information from external sources. The Company accounts for these gross to net sales adjustments in accordance with EITF Issue No. 01-9, *Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)*, and SFAS No. 48, *Revenue Recognition When Right of Return Exists*, as applicable. See "—Net Sales" section above for reconciliations of the Company's gross sales to net sales by each significant category of gross-to-net sales adjustments.

Prime vendor charge-backs

The Company's U.S. businesses participate in prime vendor programs with government entities, the most significant of which are the U.S. Department of Defense and the U.S. Department of Veterans Affairs, and other parties whereby pricing on products is extended below wholesaler list price to participating entities. These entities purchase products through wholesalers at the lower prime vendor price, and the wholesalers charge the difference between their acquisition cost and the lower prime vendor price back to the Company. The Company accounts for prime vendor charge-backs by reducing accounts receivable in an amount equal to the Company's estimate of charge-back claims attributable to a sale. The Company determines its estimate of the prime vendor charge-backs primarily based on historical experience regarding prime vendor charge-backs and current contract prices under the prime vendor programs. The Company considers prime vendor payments, levels of inventory in the distribution channel, and the Company's claim processing time lag and adjusts the reduction to accounts receivable periodically throughout each quarter to reflect actual experience.

WIC rebates

The Company's U.S. Nutritionals business participates on a competitive bidding basis in nutrition programs sponsored by states, tribal governments, the Commonwealth of Puerto Rico and the U.S. territories for Women, Infants, and Children (WIC). Under these programs, the Company reimburses these entities for the difference between wholesaler list price and the contract price on eligible products. The Company accounts for WIC rebates by establishing an accrual in an amount equal to the Company's estimate of WIC rebate claims attributable to a sale. The Company determines its estimate of the WIC rebate accrual primarily based on historical experience regarding WIC rebates and current contract prices under the WIC programs. The Company considers levels of inventory in the distribution channel, new WIC contracts, terminated WIC contracts, changes in existing WIC contracts, and WIC participation and adjusts the accrual periodically throughout each quarter to reflect actual experience.

Managed health care rebates and other contract discounts

The Company offers rebates and discounts to managed health care organizations in the U.S. and globally to other contract counterparties such as hospitals and group purchasing organizations. The Company accounts for managed health care rebates and other contract discounts by establishing an accrual in an amount equal to the Company's estimate of managed health care rebates and other contract discounts attributable to a sale. The Company determines its estimate of the managed health care rebates and other contract discounts accrual primarily based on historical experience regarding these rebates and discounts and current contract prices. The Company considers the sales performance of products subject to managed health care rebates and other contract discounts and levels of inventory in the distribution channel and adjusts the accrual periodically throughout each quarter to reflect actual experience.

Medicaid rebates

The Company's U.S. businesses participate in state government-managed Medicaid programs as well as certain other qualifying federal and state government programs whereby discounts and rebates are provided to participating state and local government entities. Discounts and rebates provided through these latter programs are included in the Company's Medicaid rebate accrual and are considered Medicaid rebates for the purposes of this discussion. The Company accounts for Medicaid rebates by establishing an accrual in an amount equal to the Company's estimate of Medicaid rebate claims attributable to a sale. The Company determines its estimate of the Medicaid rebates accrual primarily based on historical experience regarding Medicaid rebates, as well as any expansion on a prospective basis of its participation in the non-mandatory aspects of the qualifying federal and state government programs, legal interpretations of the applicable laws related to the Medicaid and qualifying federal and state government programs, and any new information regarding changes in the Medicaid programs' regulations and guidelines that would impact the amount of the rebates. The Company considers outstanding Medicaid claims, Medicaid payments, and levels of inventory in the distribution channel and adjusts the accrual periodically throughout each quarter to reflect actual experience.

Cash discounts

In the U.S. and certain other countries, the Company offers cash discounts, generally approximately 2% of the sales price, as an incentive for prompt payment. The Company accounts for cash discounts by reducing accounts receivable by the full amount of the discounts. The Company considers payment performance and adjusts the accrual to reflect actual experience.

Sales returns

The Company accounts for sales returns in accordance with SFAS No. 48 by establishing an accrual in an amount equal to the Company's estimate of sales recorded for which the related products are expected to be returned. In 2005, 2004 and 2003, provision for sales returns were \$164 million, \$276 million and \$348 million, respectively, or 1%, 1% and 2%, respectively, of gross sales.

For returns of established products, the Company determines its estimate of the sales return accrual primarily based on historical experience regarding sales returns but also considers other factors that could impact sales returns. These factors include levels of inventory in the distribution channel, estimated shelf life, product recalls, product discontinuances, price changes of competitive products, introductions of generic products and introductions of competitive new products. The Company considers all of these factors and adjusts the accrual periodically throughout each quarter to reflect actual experience.

The Company considers the level of inventory in the distribution channel and determines whether it believes an adjustment to the sales return accrual is appropriate. For example, if levels of inventory in the distribution channel increase, the Company analyzes the reasons for the increase. If the reasons indicate that sales returns will be larger than expected, the Company adjusts the sales return accrual, taking into account historical experience, the Company's returned goods policy and the shelf life of the Company's products, which ranges, on average, from approximately 12 to 48 months. In situations where the Company is aware of products in the distribution channel nearing their expiration date, the Company analyzes the situation. If the analysis indicates that sales returns will be larger than expected, the Company adjusts the sales return accrual, taking into account historical experience, the Company's returned goods policy, and levels of inventory in the distribution channel.

In the event of a product recall or product discontinuance, the Company considers the reasons for and impact of such actions and adjusts the sales return accrual as appropriate, taking into account historical experience, levels of inventory in the distribution channel and, for product discontinuances, estimates of continuing demand.

Although the Company considers price changes of competitive products, introductions of generic products and introductions of competitive new products, the Company generally does not believe that these factors impact sales returns based on historical experience and the Company's returned goods policy.

Returns from new products are significantly more difficult for the Company to assess. The Company determines its estimate of the sales return accrual primarily based on the historical sales returns experience of similar products, such as those within the same line of product or those within the same or similar therapeutic category. In limited circumstances, where the new product is not an extension of an existing line of product or where the Company has no historical experience with products in a similar therapeutic category, such that the Company cannot reliably estimate expected returns of the new product, the Company defers recognition of revenue until the right of return no longer exists or until the Company has developed sufficient historical experience to estimate sales returns. The Company also considers the shelf life of new products and determines whether it believes an adjustment to the sales return accrual is appropriate. The shelf life in connection with new products tends to be shorter than the shelf life for more established products because the Company may still be developing an optimal manufacturing process for the new product that would lengthen its shelf life, or an amount of launch quantities may have been manufactured in advance of the launch date to ensure sufficient supply exists to satisfy market demand. In those cases, the Company assesses the reduced shelf life, together with levels of inventory in the distribution channel and projected demand, and determines whether it believes an adjustment to the sales return accrual is appropriate.

Other adjustments

In addition to the significant gross to net sales adjustments described above, the Company makes other gross to net sales adjustments. For example, the Company offers sales discounts, most significantly in its non-U.S. businesses, and also offers consumer coupons and rebates, most significantly in its U.S. Nutritionals and Pharmaceuticals businesses. In addition, in a number of countries outside the U.S., including major European countries, the Company provides rebates to government entities. The Company generally accounts for these other gross to net adjustments by establishing an accrual in an amount equal to the Company's estimate of the adjustments attributable to a sale. The Company generally determines its estimates of the accruals for these other gross to net sales adjustments primarily based on historical experience, performance on commitments to government entities and other relevant factors, including levels of inventory in the distribution channel in some cases, and adjusts the accruals periodically throughout each quarter to reflect actual experience.

Use of information from external sources

The Company uses information from external sources to estimate its significant gross to net sales adjustments. The Company's estimates of inventory at the wholesalers and deferred revenue on consigned inventory are based on the projected prescription demand-based sales for its products and historical inventory experience, as well as the Company's analysis of third-party information, including written and oral information obtained from certain wholesalers with respect to their inventory levels and sell-through to customers and third-party market research data, and the Company's internal information. The inventory information received from wholesalers is a product of their record-keeping process and excludes inventory held by intermediaries to whom they sell, such as retailers and hospitals. The Company receives information from IMS Health (IMS), a supplier of market research to the pharmaceutical industry, which it uses to project the prescription demand-based sales for many of its U.S. Pharmaceutical products. The Company has historically reported estimated total U.S. prescription growth and estimated therapeutic category share based on National Prescription Audit (NPA) data, which IMS makes available to the public on a subscription basis, and a simple average of the estimated number of prescriptions in the retail and mail order channels. In the third quarter of 2005, the Company began disclosing estimated total U.S. prescription growth and estimated therapeutic category share based on both NPA and Next-Generation Prescription Services (NGPS) data. NGPS data are collected by IMS under a new, revised methodology and have been released by IMS on a limited basis through a pilot program. IMS has publicly announced that it expects to make NGPS data available to the public on a subscription basis in 2007. The Company believes that the NGPS data provided by IMS provide a superior estimate of prescription data for the Company's products in the retail and mail order channels. The Company has calculated the estimated total U.S. prescription growth and the estimated therapeutic category share based on NGPS data on a weighted average basis to reflect the fact that mail order prescriptions include a greater volume of product supplied compared with retail prescriptions. The Company believes that calculation of the estimated total U.S. prescription growth and the estimated therapeutic category share based on the NGPS data and the weighted average approach with respect to the retail and mail order channels provide a superior estimate of total prescription demand. The Company now uses this methodology for its internal demand forecasts. The Company also uses information from external sources to identify prescription trends, patient demand and average selling prices. The Company's estimates are subject to inherent limitations of estimates that rely on third-party information, as certain third-party information was itself in the form of estimates, and reflect other limitations including lags between the date as of which third-party information is generated and the date on which the Company receives third-party information.

Retirement Benefits

The Company's pension plans and postretirement benefit plans are accounted for using actuarial valuations required by SFAS No. 87, *Employers' Accounting for Pensions*, and SFAS No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*. The Company considers accounting for retirement plans critical because management is required to make significant subjective judgments about a number of actuarial assumptions, including discount rates, salary growth, long-term return on plan assets, retirement, turnover, health care cost trend rates, and mortality rates. Depending on the assumptions and estimates used, the pension and postretirement benefit expense could vary within a range of outcomes and have a material effect on reported earnings. In addition, the assumptions can materially affect accumulated benefit obligations and future cash funding.

Plan Description

The Company and certain of its subsidiaries have defined benefit pension plans, defined contribution plans, and termination indemnity plans for regular full-time employees. The principal defined benefit pension plan is the Bristol-Myers Squibb Retirement Income Plan and the principal defined contribution plan is the Bristol-Myers Squibb Savings and Investment Program.

Approximately 80% of total Company defined benefit pension plan assets and liabilities are held in U.S. plans. The assets for the U.S. plans are held in a single trust with a common asset allocation. Unless specified otherwise, the references in this section are to total Company plans (i.e., U.S. plans together with international plans).

Benefits under the Company's defined benefit pension plans are based primarily on years of credited service and on participants' compensation. Assets under the Company's defined benefit plans consist primarily of equity and fixed-income securities. At December 31, 2005, the fair market value of plan assets for the Company's defined benefit plans increased to \$5,017 million from \$4,602 million at December 31, 2004. For the U.S. plans, assets were allocated 68% to equity securities (compared to 70% at the end of 2004), 25% to fixed income securities (compared to 23% at the end of 2004) and 7% to private equity and other investments (compared to 7% at the end of 2004). Bristol-Myers Squibb common stock represented less than 1% of assets for the U.S. plans at the end of 2005 and 2004.

The Company provides comprehensive medical and group life benefits for substantially all U.S. retirees who elect to participate in the Company's comprehensive medical and group life plans. The asset allocation for these postretirement plans is identical to the asset allocation described above for the U.S. defined benefit pension plans.

Accrual Accounting and Significant Assumptions

Consistent with the requirements of SFAS No. 87, *Employers' Accounting for Pensions*, the Company accounts for pension benefits using the accrual method, recognizing pension expense before the payment of benefits to retirees. The accrual method of accounting for pension benefits necessarily requires actuarial assumptions concerning future events that will determine the amount and timing of the benefit payments.

The Company's key assumptions used in calculating its cost of pension benefits are the discount rate, the rate of compensation increase, and the expected long-term rate of return on plan assets. The Company, in consultation with its actuaries, evaluates the key actuarial assumptions and other assumptions used in calculating its cost of pension benefits, such as retirement, turnover and mortality rates, based on expectations or actual experience, as appropriate, and determines such assumptions on December 31 of each year to calculate liability information as of that date and pension expense for the following year. Depending on the assumptions used, the pension expense could vary within a range of outcomes and have a material effect on reported earnings. In addition, the assumptions can materially affect accumulated benefit obligations and future cash funding. Actual results in any given year may differ from those estimated because of economic and other factors.

In determining the discount rate, the Company uses the yield on high quality corporate bonds that coincides with the cash flows of its plans' estimated payouts. The Citigroup Above Median yield curve is used in determining the discount rate for the U.S. plans. The assumed rate of compensation increase used by the Company for determining future pension obligations reflects an estimate of the change in actual future compensation levels due to general price levels, productivity, seniority and other factors.

In 2005, net pension expense for the Company's defined benefit pension plans included in earnings before minority interest and income taxes was \$392 million compared to \$276 million in 2004.

The U.S. plans pension expense for 2005 was determined using a 5.75% assumed discount rate and a 3.56% assumed rate of compensation increase. The present value of benefit obligations at December 31, 2005 for the U.S. plans was determined using the same rates. If the assumed discount rate used in determining the U.S. plans pension expense for 2005 had been reduced by 0.25%, such expense would have increased by approximately \$18 million. If the assumed rate of compensation increase used in determining the U.S. plans pension expense for 2005 had been reduced by 0.25%, such expense would have decreased by approximately \$9 million. If the assumed discount rate used in determining the accumulated benefit obligation at December 31, 2005 had been reduced by 0.25%, the accumulated benefit obligation would have increased by \$128 million.

The U.S. plans pension expense for 2005 was determined using an 8.75% expected long-term rate of return on plan assets. If the expected long-term rate of return on plan assets used in determining the U.S. plans pension expense for 2005 had been reduced by 1%, such expense would have increased by \$34 million.

Actual rates of return earned on U.S. plan assets for each of the last 10 years were as follows:

Year	Return	Year	Return
2005	9.8%	2000	3.5%
2004	12.6%	1999	18.2%
2003	25.0%	1998	13.3%
2002	(13.4)%	1997	22.2%
2001	(6.1)%	1996	17.0%

As discussed below, GAAP provides that differences between expected and actual returns are recognized over the average future service of employees.

At December 31, 2005, the Company maintained its assumed discount rate for U.S. plans at 5.75% and maintained its assumed rate of compensation increase at 3.56%. Compensation is assumed to increase on a scale with different rates for different ages. The 3.56% rate disclosed at December 31, 2005 is the single rate which, if used at each age, would produce the same present value of benefit obligations.

The Company reduced the expected rate of return on U.S. plan assets from 9% in 2004 to 8.75% for 2005 and 2006.

The Company expects that the net pension expense for its defined benefit pension plans included in earnings before minority interest and income taxes will be approximately \$30 million lower in 2006 than the \$392 million in 2005, reflecting primarily the positive delayed impact of the favorable 2003-2005 investment returns.

The Company has used the same assumed discount rates and expected long-term rates of return on plan assets in calculating its cost of pension benefits and its cost of other postretirement benefits for U.S. plans except in the case of the discount rates at December 31, 2005 and 2004. A rate of 5.75% was used for pension benefits versus 5.50% for other postretirement benefits to reflect the shorter duration of the other postretirement liabilities.

U.S. health care costs for the retiree population are assumed to increase 8.0% in 2006 and then trend down to an expected increase of 4.5% per year by 2012. If actual costs are higher than those assumed, this will likely put significant upward pressure on the Company's expense for retiree health care.

On December 8, 2003, President Bush signed into law the Medicare Prescription Drug, Improvement and Modernization Act of 2003. The effects of the Medicare Act are reflected in 2005 net periodic postretirement benefit cost (a reduction of \$11 million) and accumulated postretirement benefit obligation at December 31, 2005 (a reduction of \$85 million).

Delayed Recognition of Actuarial Gains and Losses

At December 31, 2005 and 2004, unrecognized net actuarial losses for the Company's defined benefit plans were \$2,067 million and \$2,017 million, respectively, based on the fair market value of plan assets. These unrecognized net actuarial losses reflect in large part the steady reduction of the weighted-average discount rate over the years.

SFAS No. 87 provides for delayed recognition of actuarial gains and losses, including amounts arising from changes in the estimated plan benefit obligations due to changes in the assumed discount rate, differences between the actual and expected returns on plan assets, and other assumption changes. SFAS No. 87 requires that unrecognized net actuarial gain or loss, determined based on the market-related value of plan assets (which differs from fair market value and is a calculated value that recognizes changes in fair value in a systematic and rational manner over not more than five years), be amortized in pension income or expense for the year to the extent that such unrecognized net actuarial loss or gain exceeds 10% of the greater of the projected benefit obligation or the market-related value of plan assets at the beginning of the year. These net gains and losses are recognized as pension income or expense prospectively over a period that approximates the average remaining service period of active employees expected to receive benefits under the plans (approximately 10 years) to the extent that they are not offset by losses and gains in subsequent years.

At December 31, 2005, the unrecognized net actuarial loss, determined based on the market-related value of plan assets, was \$2,107 million. This amount exceeded 10% of the greater of the projected benefit obligation or the market related value of plan assets by \$1,515 million. Unless offset by future unrecognized gains from higher discount rates or higher than expected returns on plan assets, amortization of this unrecognized loss is expected to increase pension expense for each of the following 10 years by approximately \$152 million per year. At December 31, 2004, the unrecognized net actuarial loss, determined based on the market-related value of plan assets, was \$2,278 million. This amount exceeded 10% of the greater of the projected benefit obligation or the market related value of plan assets by \$1,730 million.

In the event the fair market value of pension plan assets of a particular plan is less than the accumulated benefit obligation for such plan at year-end, GAAP may require an additional minimum liability, and in such circumstances, a reduction in stockholders' equity or an establishment of an intangible asset. At December 31, 2005, the fair market value of the Company's defined benefit pension plan assets was \$5,017 million and the related accumulated benefit obligation was \$5,209 million. The Company recognized a reduction of \$21 million in additional minimum liability (cumulatively \$328 million) at December 31, 2005, which was offset by a \$20 million increase in other comprehensive income included in stockholders' equity and a \$1 million reduction in the intangible asset. At December 31, 2004, the fair market value of the Company's defined benefit pension plan assets was \$4,602 million and the related accumulated benefit obligation was \$4,828 million. The Company recognized an additional minimum liability of \$146 million (cumulatively \$349 million) at December 31, 2004, which was offset by a \$153 million charge to other comprehensive income included in stockholders' equity and a \$7 million reduction in the intangible asset.

Plan Funding

The Company's funding policy for defined benefit plans is to contribute amounts to provide for current service and to fund past service liability. The Company contributed \$423 million and \$367 million to the defined benefit plans in 2005 and 2004, respectively.

For discussions on retirement benefits, see Note 19 "Pension and Other Postretirement Benefit Plans."

Acquired In-Process Research and Development

The fair value of in-process research and development acquired in a business combination is determined by independent appraisal based on the present value of each research project's projected cash flows. An income approach is utilized that is consistent with guidance in the practice aid issued by the American Institute of Certified Public Accountants, *Assets Acquired in a Business Combination to Be Used in Research and Development Activities: A Focus on Software, Electronic Devices and Pharmaceutical Industries*. Future cash flows are predominately based on the net income forecast of each project, consistent with historical pricing, margins, and expense levels of similar products. Revenues are estimated based on relevant market size and growth factors, expected industry trends, individual project life cycles, and the life of each research project's underlying patent. In determining the fair value of each research project, expected revenues are first adjusted for technical risk of completion. The resulting cash flows are then discounted at a rate approximating the Company's weighted average cost of capital. Other acquired in-process research and development is expensed as incurred when the underlying product has not received regulatory approval and does not have any future alternative use. In addition, costs that are nonrefundable, related to the acquisition or licensing of products that have not yet received regulatory approval to be marketed and that have no alternative future use, are charged to earnings as incurred.

For discussions on acquired in-process research and development, see Note 1 "Accounting Policies—Acquired In-Process Research and Development."

Impairment of Long-Lived Assets

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, the Company periodically evaluates whether current facts or circumstances indicate that the carrying value of its depreciable assets to be held and used may not be recoverable. If such circumstances are determined to exist, an estimate of undiscounted future cash flows produced by the long-lived asset, or the appropriate grouping of assets, is compared to the carrying value to determine whether an impairment exists. If an asset is determined to be impaired, the loss is measured based on the difference between the asset's fair value and its carrying value. An estimate of the asset's fair value is based on quoted market prices in active markets, if available. If quoted market prices are not available, the estimate of fair value is based on various valuation techniques, including a discounted value of estimated future cash flows. The Company reports an asset to be disposed of at the lower of its carrying value or its estimated net realizable value.

In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, goodwill is tested at least annually for impairment using a two-step process. The first step is to identify a potential impairment, and the second step measures the amount of the impairment loss, if any. Goodwill is deemed to be impaired if the carrying amount of a reporting unit's goodwill exceeds its estimated fair value. SFAS No. 142 requires that indefinite-lived intangible assets be tested for impairment using a one-step process, which consists of a comparison of the fair value to the carrying value of the intangible asset. Such intangible assets are deemed to be impaired if their net book value exceeds their estimated fair value. All other intangible assets are evaluated for impairment in accordance with SFAS No. 144 as described above.

The estimates of future cash flows, based on reasonable and supportable assumptions and projections, require management's judgment. Any changes in key assumptions about the Company's businesses and their prospects, or changes in market conditions, could result in an impairment charge.

For discussions on impairment of long-lived assets, see Note 1 "Accounting Policies—Impairment of Long-Lived Assets and Goodwill and Other Intangible Assets."

Equity Investments

The Company reviews its equity investments for impairment based on its determination of whether the decline in market value of the investment below the Company's carrying value is other than temporary. In making this determination, the Company considers APB Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock* and related interpretations, which set forth factors to be evaluated in determining whether a loss in value should be recognized, including the Company's ability to hold its investment, the market price and market price fluctuations of the investment's publicly traded shares and inability of the investee to sustain an earnings capacity, which would justify the carrying amount of the investment. The Company's investment in ImClone is subject to this accounting. See Note 2 "Alliances and Investments" for a discussion of the Company's investment in ImClone.

For discussions on equity investments, see Note 1 "Accounting Policies—Investments" and Note 2 "Alliances and Investments."

Restructuring

To downsize and streamline operations and rationalize manufacturing facilities, the Company has periodically recorded restructuring charges. As a result, the Company has made estimates and judgments regarding its future plans, including future termination benefits and other exit costs to be incurred when the restructuring actions take place. Actual results could vary from these estimates, resulting in an adjustment to earnings.

For discussions on restructuring, see Note 1 "Accounting Policies—Restructuring" and Note 3 "Restructuring and Other Items."

Contingencies

In the normal course of business, the Company is subject to contingencies, such as legal proceedings and claims arising out of its business, that cover a wide range of matters, including, among others, government investigations, shareholder lawsuits, product and environmental liability, and tax matters. In accordance with SFAS No. 5, *Accounting for Contingencies*, the Company records accruals for such contingencies when it is probable that a liability will be incurred and the amount of the loss can be reasonably estimated.

For discussions on contingencies, see Note 1 "Accounting Policies—Income Taxes and Contingencies"; Note 8 "Income Taxes"; and Note 20 "Legal Proceedings and Contingencies."

Income Taxes

Deferred Taxes

The Company evaluates the need for a deferred tax asset valuation allowance by assessing whether it is more likely than not that it will realize its deferred tax assets in the future. The assessment of whether or not a valuation allowance is required often requires significant judgment including the long-range forecast of future taxable income and the evaluation of tax planning strategies. Adjustments to the deferred tax valuation allowances are made to earnings in the period when such assessments are made.

The Company has recorded deferred tax assets related to U.S. foreign tax credit carryforwards of approximately \$975 million and U.S. research tax credit carryforwards of approximately \$120 million, which expire in varying amounts beginning in 2012. Realization of the foreign tax credit and research tax credit carryforwards is dependent on generating sufficient domestic-sourced taxable income prior to their expiration. Although realization is not assured, management believes it is more likely than not that these deferred tax assets will be realized. The Company anticipates increasing its level of domestic profitability over time by undertaking actions such as increasing its biologics manufacturing capacity in the U.S. While increasing domestic profitability will likely cause the Company's effective tax rate to increase, it will also further enhance the Company's ability to utilize its foreign tax credit and research tax credit carryforwards. The amount of foreign tax credit and research tax credit carryforwards considered realizable, however, could be reduced in the near term if the outcome of the Plavix litigation in the U.S. is unfavorable, and/or if the timing of generic competition for Plavix were to be accelerated. If such events occur, the Company may need to record significant additional valuation allowances against these deferred tax assets. For additional information on Plavix litigation, see Note 20 "Legal Proceedings and Contingencies."

Tax Contingencies

The Company conducts business in various countries throughout the world and is subject to tax in numerous jurisdictions. As a result of its business activities, the Company files a significant number of tax returns that are subject to examination by various tax authorities. Tax examinations are often complex as tax authorities may disagree with the treatment of items reported by the Company and may require several years to resolve. The Company establishes liabilities for possible assessments by tax authorities. Such amounts represent a reasonable provision for taxes ultimately expected to be paid, and may need to be adjusted over time as more information becomes known.

Undistributed Earnings of Foreign Subsidiaries

As of December 31, 2005, the Company had approximately \$8.4 billion of undistributed earnings of foreign subsidiaries for which taxes have not been provided as the Company has invested or expects to invest these undistributed earnings permanently offshore. If in the future these earnings are repatriated to the United States, or if the Company determines such earnings will be remitted in the foreseeable future, additional tax provisions would be required. Due to complexities in the tax laws and the assumptions that would have to be made, it is not practicable to estimate the amounts of income taxes that would have to be provided.

For discussions on income taxes, see Note 1 "Accounting Policies—Income Taxes" and Note 8 "Income Taxes."

OUTLOOK

As previously disclosed, anticipated sales declines during 2006 due to continued exclusivity losses are expected to be more or less offset by growth in net sales of the Company's growth drivers and potential new products during the same period. Additionally, gross margin is expected to stabilize in 2006 as relatively high margins realized on the sale of growth drivers and certain new products more or less offset lost margins from older products that have lost or are expected to lose exclusivity. However, earnings will be adversely affected by the Company's investments to support the introduction of new products, the loss of revenues related to the sale of a product asset, the impact of the adoption of the expensing of stock options under new accounting guidelines and the development of additional new compounds.

In addition, as previously disclosed, the Company has experienced substantial revenue losses in the last few years due to the expiration of market exclusivity protection for certain of its products. For 2006, the Company estimates reductions of net sales in the range of \$1.4 to \$1.5 billion from 2005 levels representing continuing declines in revenues of those products as well as declines in revenues of certain additional products that have lost and will continue to lose market exclusivity protection in 2003 to 2006. These products (and the years in which they lost or will lose exclusivity protection) include Glucophage IR/Glucovance/Glucophage XR in the United States (2002 to 2004), TAXOL® (paclitaxel) in Europe (2003) and Japan (2006-2013), *Pravachol* in the United States (2006) and in Europe (2002 to 2007) and *Cefzil* in the United States (2005). In 2007, revenue reductions due to exclusivity losses are anticipated to begin to moderate from 2006 levels as no major new exclusivity losses are expected. The timing and amounts of sales reductions from exclusivity losses, their realization in particular periods and the eventual levels of remaining sales revenues are uncertain and dependent on the levels of sales at the time exclusivity protection ends, the timing and degree of development of generic competition (speed of approvals, market entry and impact) and other factors.

The Company's expectations for future sales growth include substantial expected increases in sales of Plavix, which had net sales of \$3.8 billion for 2005, and is currently the Company's largest product ranked by net sales. The composition of matter patent for Plavix, which expires in 2011, is currently the subject of litigation in the United States, with a trial scheduled to begin in June 2006. Similar proceedings involving Plavix are ongoing in Canada. There are no enforcement proceedings outside the U.S. and Canada. The Company continues to believe that the patent is valid and that it is infringed, and with its alliance partner and patent-holder Sanofi, is vigorously pursuing these cases. It is not possible at this time reasonably to assess the outcome of these litigations, or if there were an adverse determination in these litigations, the timing of potential generic competition for Plavix. Apotex Inc. and Apotex Corporation (Apotex) announced that on January 2006 it had received final approval of its aNDA for clopidogrel bisulfate from the FDA. Accordingly, Apotex could decide to launch a generic product at risk at any time. Such generic competition would likely result in substantial decreases in the sales of Plavix in the United States.

As the Company adds to its product line and realigns its focus over the next several years, the Company expects to devote substantial resources in excess of historical levels to meet heightened processing standards that may be required for sterile or newly introduced products, such as biologics. As biologics become more important to the Company's product portfolio, the Company may continue to make arrangements with third party manufacturers, and expects to make substantial investments to increase its internal capacity to produce biologics on a commercial scale. In March 2006, for example, the Board of Directors approved a capital expenditure in the amount of \$660 million for the construction of an expandable, large scale multi-product bulk biologics manufacturing facility in the U.S. The facility will be modular in design in order to accommodate future expansion. In 2006 and future periods, the Company expects cash generated by its U.S. operations, together with existing cash and borrowings from the capital markets, to sufficiently cover cash needs for working capital, capital expenditures (including any substantial investments in facilities to increase and maintain the Company's capacity to provide biologics on a commercial scale, as noted above), milestone payments and dividends paid in the United States.

The Company and its subsidiaries are the subject of a number of significant pending lawsuits, claims, proceedings and investigations. There can be no assurance that there will not be an increase in the scope of these matters or that any future lawsuits, claims and proceedings will not be material to the Company. In addition, there is an increasing trend by foreign governments to scrutinize sales and marketing activities of pharmaceutical companies and there can be no assurance that any such investigation or any other investigation will not be material. It is not possible at this time reasonably to assess the final outcome of these investigations or litigations. Management continues to believe, as previously disclosed, that during the next few years, the aggregate impact, beyond current reserves, of these and other legal matters affecting the Company is reasonably likely to be material to the Company's results of operations and cash flows, and may be material to its financial condition and liquidity. The Company's expectations for the next several years described above do not reflect the potential impact of litigation on the Company's results of operations.

Special Note Regarding Forward-Looking Statements

This annual report and other written and oral statements the Company makes from time to time contain certain “forward-looking” statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. You can identify these forward-looking statements by the fact they use words such as “should”, “expect”, “anticipate”, “estimate”, “target”, “may”, “will”, “project”, “guidance”, “intend”, “plan”, “believe” and other words and terms of similar meaning and expression in connection with any discussion of future operating or financial performance. One can also identify forward-looking statements by the fact that they do not relate strictly to historical or current facts. Such forward-looking statements are based on current expectations and involve inherent risks and uncertainties, including factors that could delay, divert or change any of them, and could cause actual outcomes to differ materially from current expectations. These statements are likely to relate to, among other things, the Company’s goals, plans and projections regarding its financial position, results of operations, cash flows, market position, product development, product approvals, sales efforts, expenses, performance or results of current and anticipated products and the outcome of contingencies such as legal proceedings, and financial results, which are based on current expectations that involve inherent risks and uncertainties, including internal or external factors that could delay, divert or change any of them in the next several years. The Company has included important factors in the cautionary statements included in this annual report that the Company believes could cause actual results to differ materially from any forward-looking statement.

Although the Company believes it has been prudent in its plans and assumptions, no assurance can be given that any goal or plan set forth in forward-looking statements can be achieved and readers are cautioned not to place undue reliance on such statements, which speak only as of the date made. The Company undertakes no obligation to release publicly any revisions to forward-looking statements as a result of new information, future events or otherwise.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to market risk due to changes in currency exchange rates and interest rates. To reduce that risk, the Company enters into certain derivative financial instruments, when available on a cost-effective basis, to hedge its underlying economic exposure. These instruments are managed on a consolidated basis to efficiently net exposures and thus take advantage of any natural offsets. Derivative financial instruments are not used for speculative purposes. Gains and losses on hedging transactions are offset by gains and losses on the underlying exposures being hedged. Any ineffective portion of hedges is reported in earnings as it occurs.

The Company's primary foreign currency exposures on anticipated transactions, primarily intercompany inventory purchases expected to occur within the next two years, are the euro, Canadian dollar, Japanese yen, Mexican peso and Chinese yuan. The Company utilizes foreign currency forward contracts to hedge exposures on certain foreign currencies and designates these derivative instruments as cash flow hedges.

The table below summarizes the Company's outstanding foreign exchange forward contracts as of December 31, 2005. The fair value of all foreign exchange forward contracts is based on year-end currency rates. The fair value of foreign exchange forward contracts should be viewed in relation to the fair value of the underlying hedged transactions and the overall reduction in exposure to adverse fluctuations in foreign currency exchange rates.

Dollars in Millions, Except Currency Rates	Weighted Average Strike Price	Notional Amount	Fair Value	Maturity
Foreign Exchange Forwards:				
Australian Dollar	.73	\$ 103	\$ —	2006
Brazilian Real	2.78	38	(4)	2006
Canadian Dollar	1.30	245	(31)	2006/2007
Euro	1.26	1,751	85	2006/2007
Polish Zloty	3.57	25	(2)	2006
Swiss Franc	1.20	56	4	2006/2007
All Others	—	78	1	2006/2007
Total Contracts		\$ 2,296	\$ 53	

At December 31, 2005, the Company held foreign exchange forward contracts with maturity dates from 2006 to 2007. At December 31, 2005 the Company did not hold any option contracts. The notional amounts and fair values of the foreign exchange forward contract maturity dates are expressed in the table below:

Year of Maturity	Notional Amount (Dollars in Millions)	Fair Value (Dollars in Millions)
2006	\$ 1,630	\$ 35
2007	666	18

At December 31, 2005, the Company held foreign exchange forward contracts with an aggregate notional amount of \$2,296 million. The fair value of the foreign exchange forward contracts was \$53 million, of which \$94 million was recorded as a non-current asset and \$41 million was recorded as a current liability. These contracts primarily related to exposures in euro, Canadian dollar and Australian dollar. The Company estimates that a 10% appreciation or depreciation in the underlying currencies being hedged from their levels against the dollar as of December 31, 2005, with all other variables held constant, would decrease or increase, respectively, by \$230 million, the fair value of foreign exchange forward contracts held at December 31, 2005.

The Company is obligated to settle foreign exchange forward contracts based on the specified contract rates. As of December 31, 2005, the balance of deferred net after-tax gains of foreign exchange forward contracts included in accumulated other comprehensive income was \$40 million, of which \$26 million is estimated to be reclassified into earnings within the next 12 months.

At December 31, 2004, the Company held option and foreign exchange forward contracts with an aggregate notional amount and fair value of \$3,461 million and \$362 million liability, respectively. These contracts primarily related to exposures in euro, Canadian dollar, Australian dollar, Swiss franc and British pound. During 2005, the Company reclassified deferred losses of \$130 million from other comprehensive income to earnings, the majority of which was classified as cost of products sold.

For the years ended December 31, 2005 and 2004, the impact of hedge ineffectiveness on earnings were not significant. Additionally, the Company uses foreign exchange forward contracts to offset its exposure to certain currency assets and liabilities. These foreign exchange forward contracts are not designated as hedges and, therefore, changes in the fair value of these derivatives are recognized in earnings as they occur. In 2005 and 2004, the amounts recognized in earnings related to foreign exchange forward contracts that did not qualify for hedge accounting treatment were not significant.

The Company also uses foreign exchange forward contracts to hedge foreign currency denominated monetary assets and liabilities. The primary objective of these foreign exchange forward contracts is to protect the U.S. dollar value of foreign currency denominated monetary assets and liabilities from the effects of volatility in foreign exchange rates that might occur prior to their receipt or settlement in U.S. dollars. These foreign currency denominated monetary assets and liabilities are primarily denominated in Japanese yen and euro. The foreign exchange forward contracts are not designated as hedges and are marked to market through other income/expense. The notional and fair value amount of purchased foreign exchange forward contracts was \$142 million and a \$2 million liability, respectively, at December 31, 2005, and was \$229 million and a \$10 million liability, respectively, at December 31, 2004. The notional and fair value amount of sold foreign exchange forward contracts was \$47 million and a \$1 million asset, respectively, at December 31, 2005, and was \$96 million and a \$4 million asset, respectively, at December 31, 2004.

In addition to the foreign exchange forward contracts noted above, the Company uses non U.S. dollar borrowings and, to a lesser extent, foreign exchange forward contracts, to hedge the foreign currency exposures of the Company's net investment in certain foreign affiliates. These non U.S. dollar borrowings and foreign exchange forward contracts are designated as hedges of net investments. The effective portion of foreign exchange gains or losses on these hedges is recorded as part of the foreign currency translation component of other comprehensive income. At December 31, 2005 and 2004, \$12 million in after tax gains and \$6 million in after tax losses, respectively, were recorded in the foreign currency translation component of other comprehensive income.

The Company uses derivative instruments as part of its interest rate risk management strategy. The derivative instruments used include interest rate swaps, which are subject to fair-value hedge accounting treatment. During 2004, 2003 and 2002 the Company executed several fixed to floating interest rate swaps to convert \$6.2 billion of the Company's fixed rate debt to be paid in 2006, 2008, 2011, 2013, 2023 and 2026 to variable rate debt. For the year ended December 31, 2005, the Company recognized a net reduction in interest expense of \$54 million that reflects the benefit of the lower floating rate obtained in the swap agreement. In April 2005, in connection with the early redemption of its \$2.5 billion Notes due 2006, the Company terminated \$2 billion notional amount of its 2006 fixed-to-floating interest rate swap agreements and incurred a pre-tax loss of \$28 million. In June 2005, the Company terminated \$500 million notional amount of its 2011 fixed-to-floating interest rate swap agreements related to its \$2.5 billion Notes due 2011, and incurred a pre-tax loss of \$23 million. This loss will be amortized to interest expense over the remaining life of the Notes, due 2011, of which \$2 million was recognized in 2005. In September 2005, the Company terminated \$350 million notional amount of its 2026 fixed-to-floating interest rate swap agreements related to its \$350 million Debentures due 2026 and resulted in a gain of \$39 million. This gain will be recognized against interest expense over the remaining life of the Debentures due 2026, of which approximately \$1 million was recognized in 2005.

SFAS No. 133 requires the revaluation, at fair value, of the swap contracts as well as the underlying debt being hedged. As such, the swap contracts and the underlying debt have been revalued resulting in an increase in non-current assets of \$21 million, current liabilities of \$51 million and a reduction in long-term debt of \$30 million, and an increase in non-current assets of \$76 million, current liabilities of \$1 million and long-term debt of \$75 million at December 31, 2005 and 2004, respectively. Swap contracts are generally held to maturity and are not used for speculative purposes. The following table summarizes the interest rate swaps outstanding as of December 31, 2005:

Interest Rate Contracts	Notional Amount of Underlying Debt	Variable Rate Received	Maturity	Fair Value
Dollars in Millions				
Swaps associated with 4.00% Notes due 2008	\$ 400	1 month U.S. \$ LIBOR +0.35%	2008	\$ (11)
Swaps associated with 5.75% Notes due 2011	2,000	1 month U.S. \$ LIBOR +1.32%	2011	(40)
Swaps associated with 5.25% Notes due 2013	600	1 month U.S. \$ LIBOR +0.42%	2013	—
Swaps associated with 7.15% Notes due 2023	350	1 month U.S. \$ LIBOR +1.66%	2023	21
	<u>\$ 3,350</u>			<u>\$ (30)</u>

At December 31, 2004, the Company held interest rate swap contracts with a notional value of \$6,200 million and a fair value of \$75 million.

It is estimated that an increase or decrease of 50 basis points in short-term or long-term interest rates would not have a material impact on the Company's consolidated financial position, results of operations or cash flows.

The Company had \$8,364 million and \$8,463 million of long-term debt outstanding at December 31, 2005 and 2004, respectively. For additional information, see Note 14 "Short-Term Borrowings and Long-Term Debt" and Note 16 "Financial Instruments."

The Company maintains cash, cash equivalents and marketable securities with various financial institutions, in order to limit exposure to any one financial institution. These financial institutions are headquartered primarily in North America and Europe.

Consolidated Statements of Earnings

	Year Ended December 31		
Dollars and Shares in Millions, Except Per Share Data	2005	2004	2003
EARNINGS			
Net Sales	\$ 19,207	\$ 19,380	\$ 18,653
Cost of products sold	5,928	5,989	5,406
Marketing, selling and administrative	5,106	5,016	4,620
Advertising and product promotion	1,476	1,411	1,415
Research and development	2,746	2,500	2,279
Acquired in-process research and development	—	63	—
Provision for restructuring, net	32	104	26
Litigation charges, net	269	420	199
Gain on sale of business	(569)	(320)	—
Equity in net income of affiliates	(334)	(273)	(151)
Other expense, net	37	52	179
Total expenses	14,691	14,962	13,973
Earnings from Continuing Operations Before Minority Interest and Income Taxes	4,516	4,418	4,680
Provision for income taxes	932	1,519	1,210
Minority interest, net of taxes	592	521	373
Earnings from Continuing Operations	2,992	2,378	3,097
Discontinued Operations			
Net earnings	(5)	10	9
Net gain on disposal	13	—	—
	8	10	9
Net Earnings	\$ 3,000	\$ 2,388	\$ 3,106
Earnings per Common Share			
Basic			
Earnings from Continuing Operations	\$ 1.53	\$ 1.23	\$ 1.60
Discontinued Operations	—	—	—
Net earnings	—	—	—
Net gain on disposal	—	—	—
Net Earnings	\$ 1.53	\$ 1.23	\$ 1.60
Diluted			
Earnings from Continuing Operations	\$ 1.52	\$ 1.21	\$ 1.59
Discontinued Operations	—	—	—
Net earnings	—	—	—
Net gain on disposal	—	—	—
Net Earnings	\$ 1.52	\$ 1.21	\$ 1.59
Average Common Shares Outstanding			
Basic	1,952	1,942	1,937
Diluted	1,983	1,976	1,950
Dividends declared per common share	\$ 1.12	\$ 1.12	\$ 1.12

The accompanying notes are an integral part of these financial statements.

Consolidated Statements of Comprehensive Income and Retained Earnings

Dollars in Millions	2005	2004	2003
COMPREHENSIVE INCOME			
Net Earnings	\$ 3,000	\$ 2,388	\$ 3,106
Other Comprehensive Income:			
Foreign currency translation, net of tax liability of \$3 in 2005, and tax benefit of \$48 in 2004 and \$25 in 2003	(270)	208	233
Deferred gains/(losses) on derivatives qualifying as hedges, net of tax liability of \$122 in 2005 and \$1 in 2004, and tax benefit of \$65 in 2003	325	(51)	(171)
Minimum pension liability adjustment, net of tax benefit of \$4 in 2005, \$42 in 2004 and \$17 in 2003	(6)	(93)	(36)
Available for sale securities, net of tax benefit of \$12 in 2005, zero in 2004, and net of tax liability of \$13 in 2003	(22)	(1)	23
Total Other Comprehensive Income	27	63	49
Comprehensive Income	\$ 3,027	\$ 2,451	\$ 3,155
RETAINED EARNINGS			
Retained Earnings, January 1	\$ 19,651	\$ 19,439	\$ 18,503
Net earnings	3,000	2,388	3,106
Cash dividends declared	(2,187)	(2,176)	(2,170)
Retained Earnings, December 31	\$ 20,464	\$ 19,651	\$ 19,439

The accompanying notes are an integral part of these financial statements.

Consolidated Balance Sheets

	December 31,	
Dollars in Millions	2005	2004
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 3,050	\$ 3,680
Marketable securities	2,749	3,794
Receivables, net of allowances of \$207 and \$221	3,378	4,373
Inventories, including consignment inventory	2,060	1,830
Deferred income taxes, net of valuation allowances	776	805
Prepaid expenses	270	319
Total Current Assets	12,283	14,801
Property, plant and equipment, net	5,693	5,765
Goodwill	4,823	4,905
Other intangible assets, net	1,921	2,260
Deferred income taxes, net of valuation allowances	1,808	1,129
Prepaid pension	1,324	1,280
Other assets	286	295
Total Assets	\$ 28,138	\$ 30,435
LIABILITIES		
Current Liabilities:		
Short-term borrowings	\$ 231	\$ 1,883
Accounts payable	1,579	2,127
Accrued expenses	2,446	2,838
Accrued rebates and returns	1,056	1,209
U.S. and foreign income taxes payable	538	1,023
Dividends payable	547	545
Accrued litigation liabilities	493	186
Deferred revenue on consigned inventory	—	32
Total Current Liabilities	6,890	9,843
Pension liabilities and other postretirement liabilities	804	832
Deferred income	241	408
Other liabilities	631	687
Long-term debt	8,364	8,463
Total Liabilities	16,930	20,233
Commitments and contingencies (Note 20)		
STOCKHOLDERS' EQUITY		
Preferred stock, \$2 convertible series: Authorized 10 million shares; issued and outstanding 6,540 in 2005 and 7,476 in 2004, liquidation value of \$50 per share	—	—
Common stock, par value of \$.10 per share: Authorized 4.5 billion shares; 2,205 million issued in 2005 and 2,202 million issued in 2004	220	220
Capital in excess of par value of stock	2,528	2,491
Restricted stock	(71)	(57)
Accumulated other comprehensive loss	(765)	(792)
Retained earnings	20,464	19,651
	22,376	21,513
Less cost of treasury stock — 248 million common shares in 2005 and 255 million in 2004	(11,168)	(11,311)
Total Stockholders' Equity	11,208	10,202
Total Liabilities and Stockholders' Equity	\$ 28,138	\$ 30,435

The accompanying notes are an integral part of these financial statements.

Consolidated Statements of Cash Flows

	Year Ended December 31,		
Dollars in Millions	2005	2004	2003
Cash Flows From Operating Activities:			
Net earnings	\$ 3,000	\$ 2,388	\$ 3,106
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Depreciation	577	593	491
Amortization	352	316	298
Deferred income tax benefits	(812)	278	249
Litigation settlement expense, net of recoveries	269	420	199
Provision for restructuring	32	104	29
Gain on sale of businesses	(632)	(320)	—
Deferred income recognized	(143)	—	—
Acquired in-process research and development	—	63	—
Impairment charges and asset write-offs	42	—	26
Loss/(gain) on disposal of property, plant and equipment and investment in other companies	36	18	(3)
Undistributed losses of affiliates, net	50	7	66
Unfunded pension expense	(31)	(91)	(195)
Changes in operating assets and liabilities:			
Receivables	539	(556)	(549)
Inventories	(370)	(133)	127
Prepaid expenses	30	2	50
Other assets	8	16	(70)
Deferred revenue on consigned inventory	(32)	(44)	(394)
Litigation settlement payments, net of insurance recoveries	11	(500)	(526)
Accounts payable and accrued expenses	(378)	248	394
Product liability	(48)	38	(3)
U.S. and foreign income taxes payable	(534)	228	147
Other liabilities	(130)	101	70
Net Cash Provided by Operating Activities	1,836	3,176	3,512
Cash Flows From Investing Activities:			
Purchases, net of sales and maturities, of marketable securities	1,043	(779)	(1,385)
Additions to property, plant and equipment and capitalized software	(738)	(676)	(937)
Proceeds from disposal of property, plant and equipment and investment in other companies	73	35	59
Proceeds from sale of businesses/product lines	843	364	—
Purchase of Acordis Speciality Fibres	—	(150)	—
ImClone milestone payment	—	(250)	—
Purchases of trademarks, patents, licenses and other businesses	—	(133)	(53)
Divestiture and acquisition costs	—	(29)	(18)
Investments in other companies	(30)	(4)	(85)
Net Cash Provided by/(Used in) Investing Activities	1,191	(1,622)	(2,419)
Cash Flows From Financing Activities:			
Short-term (repayments)/borrowings	(1,625)	1,558	(1,189)
Long-term debt borrowings	2,510	15	2,286
Long-term debt repayments	(2,502)	(3)	(3)
Issuances of common stock under stock plans	166	141	44
Dividends paid	(2,186)	(2,174)	(2,169)
Net Cash Used in Financing Activities	(3,637)	(463)	(1,031)
Effect of Exchange Rates on Cash and Cash Equivalents	(20)	40	36
(Decrease)/Increase in Cash and Cash Equivalents	(630)	1,131	98
Cash and Cash Equivalents at Beginning of Period	3,680	2,549	2,451
Cash and Cash Equivalents at End of Period	\$ 3,050	\$ 3,680	\$ 2,549

The accompanying notes are an integral part of these financial statements.

Note 1 Accounting Policies

Basis of Consolidation

The consolidated financial statements include the accounts of Bristol-Myers Squibb Company (BMS, the Company or Bristol-Myers Squibb) and all of its controlled majority-owned subsidiaries. All intercompany balances and transactions have been eliminated. Certain prior year amounts have been reclassified to conform to the current year presentation.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The most significant assumptions are employed in estimates used in determining values of intangible assets, restructuring charges and accruals, sales rebate and return accruals, legal contingencies and tax assets and tax liabilities, as well as in estimates used in applying the revenue recognition policy and accounting for retirement and postretirement benefits (including the actuarial assumptions). Actual results may or may not differ from estimated results.

Revenue Recognition

The Company recognizes revenue in accordance with Staff Accounting Bulletin (SAB) No. 101, *Revenue Recognition in Financial Statements*, as amended by SAB No. 104, *Revenue Recognition*, when substantially all the risks and rewards of ownership have transferred to the customer. Generally, revenue is recognized at time of shipment. However, in the case of certain sales made by the Nutritionals and Other Health Care segments and certain non-U.S. businesses within the Pharmaceuticals segment, revenue is recognized on the date of receipt by the purchaser. Revenues are reduced at the time of recognition to reflect expected returns that are estimated based on historical experience. Additionally, provisions are made at the time of revenue recognition for all discounts, rebates and estimated sales allowances based on historical experience updated for changes in facts and circumstances, as appropriate. Such provisions are recorded as a reduction of revenue.

In the case of sales made to wholesalers (1) as a result of incentives, (2) in excess of the wholesaler's ordinary course of business inventory level, (3) at a time when there was an understanding, agreement, course of dealing or consistent business practice that the Company would extend incentives based on levels of excess inventory in connection with future purchase, and (4) at a time when such incentives would cover substantially all, and vary directly with, the wholesaler's cost of carrying inventory in excess of the wholesaler's ordinary course of business inventory level, substantially all the risks and rewards of ownership do not transfer upon shipment, and accordingly, such sales were accounted for using the consignment model. The determination of when, if at all, sales to a wholesaler meet the foregoing criteria involves evaluation of a variety of factors and a number of complex judgments. Under the consignment model, the Company does not recognize revenue upon shipment of product. Rather, upon shipment of product the Company invoices the wholesaler, records deferred revenue at gross invoice sales price, and classifies the inventory held by the wholesalers as consignment inventory at the Company's cost of such inventory. The Company recognizes revenue when the consignment inventory is no longer subject to incentive arrangements but not later than when such inventory is sold through to the wholesalers' customers, on a first-in first-out (FIFO) basis.

In the case of new products for which the product introduction is not an extension of an existing line of product, where the Company determines that there are not products in a similar therapeutic category, or where the Company determines the new product has dissimilar characteristics with existing products, such that the Company cannot reliably estimate expected returns of the new product, the Company defers recognition of revenue until the right of return no longer exists or until the Company has developed sufficient historical experience to estimate sales returns.

Sales Rebate and Return Accruals

Medicaid rebate accruals were \$326 million and \$372 million at December 31, 2005 and 2004, respectively; Women, Infants and Children (WIC) rebate accruals were \$252 million and \$234 million, respectively; and managed health care rebate and other contractual discount accruals were \$167 million and \$198 million at December 31, 2005 and 2004, respectively. These and other rebate accruals were established in the same period the related revenue was recognized, resulting in a reduction to sales and the establishment of a liability, which is included in accrued liabilities. An accrual is recorded based on an estimate of the proportion of recorded revenue that will result in a rebate or return. Prime vendor charge-back accruals, established in a similar manner, are recorded as a reduction to accounts receivable and were \$107 million and \$106 million at December 31, 2005 and 2004, respectively.

Income Taxes

Deferred Taxes

The provision for income taxes has been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or payable for the current year plus the change in deferred taxes during the year. Deferred taxes result from differences between the financial and tax bases of the Company's assets and liabilities and are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized. The assessment of whether or not a valuation allowance is required often requires significant judgment including the long-range forecast of future taxable income and the evaluation of tax planning initiatives. Adjustments to the deferred tax valuation allowances are made to earnings in the period when such assessments are made. As of December 31, 2005 and 2004, the Company had net deferred tax assets of \$2,380 million and \$1,713 million, respectively, net of valuation allowances of \$559 million and \$507 million, respectively.

The Company has recorded deferred tax assets related to U.S. foreign tax credit carryforwards and U.S. research tax credit carryforwards, which expire in varying amounts beginning in 2012. Realization of the foreign tax credit and research tax credit carryforwards is dependent on generating sufficient domestic-sourced taxable income prior to their expiration. Although realization is not assured, management believes it is more likely than not that these deferred tax assets will be realized. The Company anticipates increasing its level of domestic profitability over time by undertaking actions such as increasing its biologics manufacturing capacity in the U.S. While increasing domestic profitability will likely cause the Company's effective tax rate to increase, it will also further enhance the Company's ability to utilize its foreign tax credit and research tax credit carryforwards. The amount of foreign tax credit and research tax credit carryforwards considered realizable, however, could be reduced in the near term if the outcome of the Plavix litigation in the U.S. is unfavorable, and/or if the timing of generic competition for Plavix were to be accelerated. If such events occur, the Company may need to record significant additional valuation allowances against these deferred tax assets. For additional information on Plavix litigation, see Note 20 "Legal Proceedings and Contingencies."

Tax Benefit on Qualified Production Activities

Under the guidance of the Financial Accounting Standards Board (FASB) Staff Position (FSP) No. 109-1, *Application of FASB Statement No. 109, "Accounting for Income Taxes," to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004*, this deduction will be treated as a "special deduction" as described in Statement of Financial Accounting Standards (SFAS) No. 109. As such, the special deduction will not affect deferred tax assets and liabilities existing at the enactment date. Rather, the impact of this deduction will be reported in the period in which the deduction is claimed on the Company's tax return.

Undistributed Earnings of Foreign Subsidiaries

As of December 31, 2005, the Company had approximately \$8.4 billion of undistributed earnings of foreign subsidiaries for which taxes have not been provided, as the Company has invested or expects to invest these undistributed earnings permanently offshore. If in the future these earnings are repatriated to the United States, or if the Company determines such earnings will be remitted in the foreseeable future, additional tax provisions would be required. Due to complexities in the tax laws and the assumptions that would have to be made, it is not practicable to estimate the amounts of income taxes that would have to be provided.

Tax Contingencies

The Company conducts business in various countries throughout the world and is subject to tax in numerous jurisdictions. As a result of its business activities, the Company files a significant number of tax returns that are subject to examination by various tax authorities. Tax examinations are often complex as tax authorities may disagree with the treatment of items reported by the Company and may require several years to resolve. The Company establishes liabilities for possible assessments by tax authorities resulting from known tax exposures. Such amounts represent a reasonable provision for taxes ultimately expected to be paid, and may need to be adjusted over time as more information becomes known.

Cash and Cash Equivalents

Cash equivalents are primarily highly liquid investments with original maturities of three months or less at the time of purchase, and are recorded at cost, which approximates fair value.

Marketable Securities

The Company accounts for marketable securities in accordance with SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. The Company determined the appropriate classification of all marketable securities was "available-for-sale" at the time of purchase. As such, at December 31, 2005 and 2004, all of the Company's investments in marketable securities were reported at fair value. Unrealized gains and losses are reported as a component of accumulated other comprehensive income (loss) in stockholders' equity. The amortized cost of debt securities, held to maturity, is adjusted for amortization of premiums and accretion of discounts from the date of purchase to maturity. Such amortization is included in interest income as an addition to or deduction from the coupon interest earned on the investments. The Company follows its investment managers' method of determining the cost basis in computing realized gains and losses on the sale of its available-for-sale securities, which is the average cost method. Realized gains and losses are included in other income (expense).

Inventory Valuation

Inventories are generally stated at average cost, not in excess of market.

Capital Assets and Depreciation

Expenditures for additions, renewals and improvements are capitalized at cost. Depreciation is generally computed on a straight-line method based on the estimated useful lives of the related assets. The estimated useful lives of the major classes of depreciable assets are 50 years for buildings and 3 to 40 years for machinery, equipment and fixtures. The Company periodically evaluates whether current events or circumstances indicate that the carrying value of its depreciable assets may not be recoverable.

Impairment of Long-Lived Assets

The Company periodically evaluates whether current facts or circumstances indicate that the carrying value of its depreciable assets to be held and used may not be recoverable. If such circumstances are determined to exist, an estimate of undiscounted future cash flows produced by the long-lived asset, or the appropriate grouping of assets, is compared to the carrying value to determine whether an impairment exists. If an asset is determined to be impaired, the loss is measured based on the difference between the asset's fair value and its carrying value. An estimate of the asset's fair value is based on quoted market prices in active markets, if available. If quoted market prices are not available, the estimate of fair value is based on various valuation techniques, including a discounted value of estimated future cash flows. The Company reports an asset to be disposed of at the lower of its carrying value or its estimated net realizable value.

Capitalized Software

Certain costs to obtain internal use software for significant systems projects are capitalized and amortized over the estimated useful life of the software, which ranges from 3 to 10 years. Costs to obtain software for projects that are not significant are expensed as incurred. Capitalized software, net of accumulated amortization, included in other intangible assets, was \$336 million and \$394 million, at December 31, 2005 and 2004, respectively. Amortization expense was \$116 million, \$90 million and \$71 million for the years ended December 31, 2005, 2004 and 2003, respectively.

Investments

In January 2003, the Company adopted FASB Interpretation No. 46 (FIN 46 or Interpretation), *Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51*. FIN 46 clarifies the application of Accounting Research Bulletin (ARB) No. 51, *Consolidated Financial Statements*, to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. Such entities are known as variable interest entities (VIEs). The FASB issued a revision to FIN 46 (FIN 46-R) in December 2003. FIN 46-R is effective for the interim period ending March 31, 2004 for all new or existing VIEs. The adoption of FIN 46 had no effect on the Company's financial statements.

If an entity does not meet the definition of a VIE under FIN 46, the Company accounts for the entity under the provisions of ARB No. 51, *Consolidated Financial Statements, as amended by SFAS No. 94, Consolidation of All Majority-Owned Subsidiaries*, which requires that the Company consolidates all majority (more than 50%) owned subsidiaries where it has the ability to exercise control. The Company accounts for 50% or less owned companies over which it has the ability to exercise significant influence using the equity method of accounting. The Company's share of net income or losses of equity investments is included in equity in net income of affiliates in the consolidated statement of earnings. The Company reviews its equity investments for impairment based on its determination of whether the decline in market value of the investment below the Company's carrying value is other than temporary. In making this determination, the Company considers Accounting Principles Board (APB) Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock* and related interpretations, which set forth factors to be evaluated in determining whether a loss in value should be recognized, including the Company's ability to hold its investment, the market price and market price fluctuations of the investment's publicly traded shares and inability of the investee to sustain an earnings capacity, which would justify the carrying amount of the investment.

Long-term investments in securities, which comprise marketable equity securities and securities and investments for which market values are not readily available, are included in other assets. Marketable equity securities are classified as available-for-sale and reported at fair value. Fair value is based on quoted market prices as of the end of the reporting period. Securities and investments for which market values are not readily available are carried at cost. Unrealized gains and losses are reported, net of their related tax effects, as a component of accumulated other comprehensive income (loss) in stockholders' equity until sold. At the time of sale, any gains or losses are calculated by the specific identification method and recognized in other income (expense). Losses are also recognized in other income (expense) when a decline in market value is deemed to be other than temporary.

Goodwill and Other Intangible Assets

Goodwill is no longer amortized but is tested for impairment annually using a two-step process. The first step is to identify a potential impairment, and the second step measures the amount of the impairment loss, if any. Goodwill is deemed to be impaired if the carrying amount of a reporting unit's goodwill exceeds its estimated fair value. The Company has completed its goodwill impairment assessment, which indicated no impairment of goodwill.

Other intangible assets, consisting of patents, trademarks, technology, licenses, and capitalized software, are amortized on a straight-line basis over their useful lives, ranging from 3 to 17 years. Indefinite-lived intangible assets, if any, are tested for impairment using a one-step process, which consists of a comparison of the fair value to the carrying value of the intangible asset. Such intangible assets are deemed to be impaired if their net book value exceeds their estimated fair value. All other intangible assets are evaluated for impairment as described under "—Impairment of Long-Lived Assets" above.

Restructuring

To downsize and streamline operations and rationalize manufacturing facilities, the Company has periodically recorded restructuring charges. As a result, the Company has made estimates and judgments regarding its future plans, including future termination benefits and other exit costs to be incurred when the restructuring actions take place. Actual results may or may not vary from these estimates, resulting in potential adjustment to earnings in subsequent periods.

Product Liability

Accruals for product liability (including associated legal costs) are recorded on an undiscounted basis when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated based on existing information. These accruals are adjusted periodically as assessment efforts progress or as additional information becomes available. Receivables for related insurance or other third-party recoveries for product liabilities are recorded, on an undiscounted basis, when it is probable that a recovery will be realized and are classified as a reduction of litigation charges in the consolidated statement of earnings.

Contingencies

In the normal course of business, the Company is subject to loss contingencies, such as legal proceedings and claims arising out of its business, that cover a wide range of matters, including, among others, government investigations, shareholder lawsuits, product and environmental liability, and tax matters. In accordance with SFAS No. 5, *Accounting for Contingencies* (SFAS No. 5), the Company records accruals for such loss contingencies when it is probable that a liability will be incurred and the amount of loss can be reasonably estimated. The Company in accordance with SFAS No. 5, does not recognize gain contingencies until realized. For a discussion of contingencies, see Note 8 "Income Taxes" and Note 20 "Legal Proceedings and Contingencies."

Derivative Financial Instruments

Derivative financial instruments are used by the Company principally in the management of its interest rate and foreign currency exposures. The Company does not hold or issue derivative financial instruments for speculative purposes.

The Company records all derivative instruments on the balance sheet at fair value. Changes in a derivative's fair value are recognized in earnings unless specific hedge criteria are met. If the derivative is designated as a fair value hedge, the changes in the fair value of the derivative and of the hedged item attributable to the hedged risk are recognized in the consolidated statement of earnings. If the derivative is designated as a cash flow hedge, the effective portions of changes in the fair value of the derivative are recorded in other comprehensive income (loss) and are subsequently recognized in the consolidated statement of earnings when the hedged item affects earnings; cash flows are classified consistent with the underlying hedged item. For purchased foreign currency options the entire change in fair value is included in the measurement of hedge effectiveness for cash flow hedges. Ineffective portions of changes in the fair value of cash flow hedges, if any, are recognized as a charge or credit to earnings.

The Company designates and assigns derivatives as hedges of forecasted transactions, specific assets or specific liabilities. When hedged assets or liabilities are sold or extinguished or the forecasted transactions being hedged are no longer expected to occur, the Company immediately recognizes the gain or loss on the designated hedging financial instruments in the consolidated statement of earnings.

Shipping and Handling Costs

The Company typically does not charge customers for shipping and handling costs. Shipping and handling costs, when charged, are included in marketing, selling and administrative expenses and were \$245 million in 2005 and 2004, and \$243 million in 2003.

Advertising Costs

Advertising costs are expensed as incurred. Advertising expense was \$509 million, \$479 million and \$448 million in 2005, 2004 and 2003, respectively.

Milestone Payments

The Company from time to time will enter into strategic alliances with third parties, which give the Company rights to develop, manufacture, market and/or sell pharmaceutical products, the rights to which are owned by such third parties. As a result of these alliances, the Company may be obligated to make payments to alliance partners contingent upon the achievement of certain pre-determined criteria. For milestones achieved prior to marketing approval of the product, such payments are expensed as research and development. After product approval, any additional milestones are capitalized and amortized to cost of products sold over the remaining useful life of the asset. All capitalized milestone payments are tested for recoverability whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable.

Acquired In-Process Research and Development

The fair value of in-process research and development acquired in a business combination is determined by independent appraisal based on the present value of each research project's projected cash flows. An income approach is utilized that is consistent with guidance in the practice aid issued by the American Institute of Certified Public Accountants, *Assets Acquired in Business Combinations to Be Used in Research and Development Activities: A Focus on Software, Electronic Devices and Pharmaceutical Industries*. Future cash flows are predominately based on the net income forecast of each project, consistent with historical pricing, margins and expense levels of similar products. Revenues are estimated based on relevant market size and growth factors, expected industry trends, individual project life cycles and the life of each research project's underlying patent. In determining the fair value of each research project, expected revenues are first adjusted for technical risk of completion. The resulting cash flows are then discounted at a rate approximating the Company's weighted average cost of capital. Other acquired in-process research and development is expensed as incurred when the underlying product has not received regulatory approval and does not have any future alternative use. In addition, costs that are nonrefundable, related to the acquisition or licensing of products that have not yet received regulatory approval to be marketed and that have no alternative future use, are charged to earnings as incurred.

Earnings Per Share

Basic earnings per common share are computed using the weighted-average number of shares outstanding during the year. Diluted earnings per common share are computed using the weighted-average number of shares outstanding during the year plus the incremental shares outstanding assuming the exercise of dilutive stock options, restricted stock and convertible instruments.

Foreign Currency Translation

The net assets of the Company's foreign subsidiaries are translated into U.S. dollars using current exchange rates. The U.S. dollar effects that arise from translating the net assets of these subsidiaries at changing rates are recorded in the foreign currency translation adjustment account, which is included in other comprehensive income.

Stock Compensation Plans

In December 2004, the FASB issued revised SFAS No. 123 (SFAS No. 123R), *Share-Based Payment*. This standard eliminates the ability to account for share-based compensation transactions using the intrinsic value-based method under APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and requires instead that such transactions be accounted for using a fair-value-based method. In April 2005, the SEC delayed the effective date of SFAS No. 123R to financial statements issued for the first annual period beginning after June 15, 2005. The Company adopted SFAS No. 123R on January 1, 2006 using the prospective transition method.

As a result of the provisions in SFAS No. 123R and Staff Accounting Bulletin No. 107, the Company estimates that the compensation charges related to share-based compensation for 2006 to be on a pre-tax basis between \$135 million and \$145 million which includes \$80 million to \$85 million of stock option expense due to the adoption of this standard. On an after tax basis, the compensation charges related to share-based compensation for 2006 are estimated to be between \$85 million and \$91 million and the stock option expense due to the adoption of this standard included in these after tax amounts is \$50 million to \$54 million. However, the assessment of the estimated compensation charges is affected by the Company's stock price as well as a number of complex and subjective variables and the related tax impacts. These variables include, but are not limited to, the volatility of the Company's stock price and employee stock exercise behaviors.

With respect to the accounting treatment of retirement eligibility provisions of employee share-based compensation awards, the Company has historically followed the nominal vesting period approach. Upon the adoption of SFAS No. 123R on January 1, 2006, the Company will adopt the non-substantive vesting period approach and begin recognizing compensation cost over a one year period for awards granted to retirement eligible employees, or if more than one year over the period from the grant date to the date retirement eligibility is achieved but less than the vesting period. The adoption of the non-substantive vesting period approach is not expected to have a material effect on the consolidated financial statements.

Also in conjunction with adoption of SFAS No. 123R, the Company changed its method of attributing the value of share-based compensation to expense from the accelerated, multiple-option approach to the straight-line, single-option approach. Compensation expense for all share-based payment awards granted prior to adoption will continue to be recognized using the accelerated, multiple-option approach where permissible. Compensation expense for all share-based payment awards granted upon or subsequent to adoption of SFAS No. 123R will be recognized using the straight-line, single-option approach.

Currently, the Company applies APB Opinion No. 25, and related interpretations in accounting for its stock-based compensation plans and discloses the pro forma net income and related pro forma income per share information in accordance with SFAS No. 123, *Accounting for Stock-Based Compensation*, and SFAS No. 148, *Accounting for Stock-Based Compensation Costs—Transition and Disclosure*. The Company does not recognize compensation expense for stock options granted under the plans as the exercise price of the option on the date of grant is equal to the fair market value as of that date. For grants of restricted stock, the Company recognizes compensation expense on a straight-line basis over the period that the restrictions expire.

The following table summarizes the Company's results on a pro forma basis as if it had recorded compensation expense based upon the fair value at the grant date for awards under these plans consistent with the methodology prescribed in SFAS No. 123 for 2005, 2004 and 2003:

Dollars in Millions, Except Per Share Data	2005	2004	2003
Net Earnings:			
As reported	\$ 3,000	\$ 2,388	\$ 3,106
Total stock-based employee compensation expense, included in reported net earnings, net of related tax effects	20	19	14
Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(112)	(138)	(195)
Pro forma	\$ 2,908	\$ 2,269	\$ 2,925
Basic earnings per share:			
As reported	\$ 1.53	\$ 1.23	\$ 1.60
Pro forma	1.49	1.17	1.51
Diluted earnings per share:			
As reported	\$ 1.52	\$ 1.21	\$ 1.59
Pro forma	1.48	1.15	1.50

Options related to discontinued operations have no impact on basic and diluted earnings per share. See Note 15 "Stockholders' Equity" for additional information.

Recently Issued Accounting Standards

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections*, which replaces APB Opinion No. 20, *Accounting Changes* and SFAS No. 3, *Reporting Accounting Changes in Interim Financial Statements*. This pronouncement applies to all voluntary changes in accounting principle, and revises the requirements for accounting for and reporting a change in accounting principle. SFAS No. 154 requires retrospective application to prior periods' financial statements of a voluntary change in accounting principle, unless it is impracticable to do so. This pronouncement also requires that a change in the method of depreciation, amortization, or depletion for long-lived, non-financial assets be accounted for as a change in accounting estimate that is effected by a change in accounting principle. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The Statement does not change the transition provisions of any existing accounting pronouncements, including those that are in a transition phase as of the effective date of SFAS No. 154. The adoption of this accounting pronouncement is not expected to have a material effect on the consolidated financial statements.

In March 2005, the FASB issued FASB Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations* (FIN 47). FIN 47 clarifies that an entity must record a liability for a conditional asset retirement obligation if the fair value of the obligation can be reasonably estimated. Asset retirement obligations covered by FIN 47 are those for which an entity has a legal obligation to perform an asset retirement activity, even if the timing and method of settling the obligation are conditional on a future event that may or may not be within the control of the entity. FIN 47 also clarifies when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation. FIN 47 is effective no later than the end of fiscal years ending after December 15, 2005. The adoption of this accounting pronouncement did not have a material effect on the Company's consolidated financial statements.

In December 2004, the FASB issued revised SFAS No. 123 (SFAS No. 123R), *Share-Based Payment*. This standard eliminates the ability to account for share-based compensation transactions using the intrinsic value-based method under APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and requires instead that such transactions be accounted for using a fair-value-based method. See "—Stock Compensation Plans" above.

In December 2004, the FASB issued FSP No. 109-1—Application of SFAS No. 109, *Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004*. The FSP provides that the deduction on qualified production activities will be treated as a "special deduction" as described in SFAS No. 109, *Accounting for Income Taxes*. Accordingly, the tax effect of this deduction will be reported as a component of the Company's tax provision and will not have an effect on deferred tax assets and liabilities. The Department of the Treasury recently issued Proposed Tax Regulations with respect to the *Deduction on Qualified Production Activities*. The Company is evaluating the impact of the Proposed Tax Regulations and the FSP on its income tax provision and results of operations. See "—Income Taxes" above.

In December 2004, the FASB issued SFAS No. 153, *Exchanges of Nonmonetary Assets*. The provisions of this Statement are effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005 and should be applied prospectively. The Statement eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets in paragraph 21(b) of APB Opinion No. 29, *Accounting for Nonmonetary Transactions*, and replaces it with an exception for exchanges that do not have commercial substance. The adoption of this accounting pronouncement did not have a material effect on the Company's consolidated financial statements.

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs – an Amendment of ARB No. 43, Chapter 4*. The standard requires abnormal amounts of idle facility and related expenses to be recognized as current period charges and also requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. SFAS No. 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. The adoption of this accounting pronouncement is not expected to have a material effect on the consolidated financial statements.

In June 2004, the FASB issued FSP No. 106-2, *Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003* (the Medicare Act). The Medicare Act introduces a prescription drug benefit under Medicare as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. FSP No. 106-2 requires that the effects of the new law be accounted for under SFAS No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions*. The Company adopted FSP No. 106-2 in the third quarter of 2004, retroactive to January 1, 2004. There was a reduction in net periodic benefit cost for other benefits of \$8 million for 2004, based on the re-measurement of the accumulated postretirement benefit obligation as of January 1, 2004. The effect of the adoption of FSP No. 106-2 was not material to the Company's consolidated financial statements. See Note 19 "Pension and Other Postretirement Benefit Plans."

In March 2004, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 03-06, *Participating Securities and the Two-Class Method Under FAS 128*, which requires the use of the two-class method of computing earnings per share for those enterprises with participating securities or multiple classes of common stock. The consensus is effective for fiscal periods beginning after March 31, 2004. The adoption of EITF No. 03-06 did not have a material effect on the consolidated financial statements.

In December 2003, the FASB revised Interpretation No. 46, *Consolidation of Variable Interest Entities* (FIN 46). FIN 46 requires a variable interest entity to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity's activities or is entitled to receive a majority of the entity's residual returns or both. FIN 46 also requires disclosures about variable interest entities that a company is not required to consolidate but in which it has a significant variable interest. The consolidation requirements of FIN 46 (as revised) apply immediately to variable interest entities created after January 31, 2003 and to existing entities in the first fiscal year or interim period ending after March 15, 2004. Certain of the disclosure requirements apply to all financial statements issued after January 31, 2003, regardless of when the variable interest entity was established. The adoption of this accounting pronouncement did not have a material effect on the consolidated financial statements.

Note 2 Alliances and Investments

Sanofi-Aventis

The Company has agreements with Sanofi-Aventis (Sanofi) for the codevelopment and cocommercialization of Avapro/Avalide (irbesartan), an angiotensin II receptor antagonist indicated for the treatment of hypertension, and Plavix (clopidogrel), a platelet aggregation inhibitor. The worldwide alliance operates under the framework of two geographic territories; one in the Americas (principally the United States, Canada, Puerto Rico and Latin American countries) and Australia and the other in Europe and Asia. Accordingly, two territory partnerships were formed to manage central expenses, such as marketing, research and development and royalties, and to supply finished product to the individual countries. In general, at the country level, agreements either to copromote (whereby a partnership was formed between the parties to sell each brand) or to comarket (whereby the parties operate and sell their brands independently of each other) are in place. The agreements expire on the later of (i) with respect to Plavix, 2013 and, with respect to Avapro/Avalide, 2012 in the Americas and Australia and 2013 in Europe and Asia and (ii) the expiration of all patents and other exclusivity rights in the applicable territory.

The Company acts as the operating partner for the territory covering the Americas and Australia and owns a 50.1% majority controlling interest in this territory. Sanofi's ownership interest in this territory is 49.9%. As such, the Company consolidates all country partnership results for this territory and records Sanofi's share of the results as a minority interest, net of taxes, which was \$578 million in 2005, \$502 million in 2004 and \$351 million in 2003. The Company recorded sales in this territory and in comarketing countries outside this territory (Germany, Italy, Spain and Greece) of \$4,805 million in 2005, \$4,257 million in 2004 and \$3,224 million in 2003.

Cash flows from operating activities of the partnerships in the territory covering the Americas and Australia are recorded as operating activities within the Company's consolidated statement of cash flows. Distributions of partnership profits to Sanofi and Sanofi's funding of ongoing partnership operations occur on a routine basis and are also recorded within operating activities on the Company's consolidated statement of cash flows.

Sanofi acts as the operating partner of the territory covering Europe and Asia and owns a 50.1% majority financial controlling interest within this territory. The Company's ownership interest in the partnership within this territory is 49.9%. The Company accounts for the investment in partnership entities in this territory under the equity method and records its share of the results in equity in net income of affiliates in the consolidated statement of earnings. The Company's share of net income from these partnership entities before taxes was \$345 million in 2005, \$269 million in 2004 and \$187 million in 2003.

The Company routinely receives distributions of profits and provides funding for the ongoing operations of the partnerships in the territory covering Europe and Asia. These transactions are recorded as operating activities within the Company's consolidated statement of cash flows.

In 2001, the Company and Sanofi formed an alliance for the copromotion of irbesartan, as part of which the Company contributed the irbesartan distribution rights in the United States and Sanofi paid the Company a total of \$350 million in the two years ended December 31, 2002. The Company accounted for this transaction as a sale of an interest in a license and deferred and amortized the \$350 million to other income over the expected useful life of the license, which is approximately 11 years from the formation of the irbesartan copromotion alliance. The Company recognized other income of \$31 million, \$32 million and \$31 million in 2005, 2004 and 2003, respectively. The unamortized portion of the deferred income is recorded in the liabilities section of the consolidated balance sheet and was \$217 million and \$248 million as of December 31, 2005 and 2004, respectively.

Otsuka

The Company has a worldwide commercialization agreement with Otsuka Pharmaceutical Co., Ltd. (Otsuka), to codevelop and copromote with Otsuka Abilify (aripiprazole) for the treatment of schizophrenia and related psychiatric disorders, except in Japan, China, Taiwan, North Korea, South Korea, the Philippines, Thailand, Indonesia, Pakistan and Egypt. The Company began copromoting the product with Otsuka in the U.S. and Puerto Rico in November 2002. In June 2004, the Company received marketing approval from the European Commission. The product is currently copromoted with Otsuka in the United Kingdom, Germany and Spain. Abilify is currently distributed exclusively by the Company in France on a temporary basis until Otsuka joins the copromotion of the product. The Company records alliance revenue for its 65% contractual share of Otsuka's net sales in these copromotion countries, excluding the United Kingdom, and records all expenses related to the product. The Company recognizes this alliance revenue when Abilify is shipped and all risks and rewards of ownership have transferred to Otsuka's customers. In the United Kingdom, and in France until copromotion with Otsuka commences, the Company records 100% of the net sales and related costs of products sold.

The Company also has an exclusive right to sell Abilify in other countries in Europe, the Americas and a number of countries in Asia. In these countries the Company records 100% of the net sales and related cost of products sold. Under the terms of the agreement, the Company purchases the product from Otsuka and performs finish manufacturing for sale by the Company to its customers. The agreement expires in November 2012 in the U.S. and Puerto Rico. For the entire European Union, the agreement expires in June 2014. In each other country where the Company has the exclusive right to sell Abilify, the agreement expires on the later of the tenth anniversary of the first commercial sale in such country or expiration of the applicable patent in such country.

The Company recorded revenue for Abilify of \$912 million in 2005, \$593 million in 2004 and \$283 million in 2003. Total milestone payments made to Otsuka under the agreement through December 2005 were \$217 million, of which \$157 million was expensed as acquired in-process research and development in 1999. The remaining \$60 million was capitalized in other intangible assets and is amortized in cost of products sold over the remaining life of the agreement in the U.S., ranging from 8 to 11 years. The Company amortized in cost of products sold \$6 million in 2005, \$5 million in 2004 and \$5 million in 2003. The unamortized capitalized payment balance was \$41 million and \$47 million as of December 31, 2005 and 2004, respectively.

ImClone

The Company has a commercialization agreement expiring in September 2018 with ImClone Systems Incorporated (ImClone), a biopharmaceutical company focused on developing targeted cancer treatments, for the codevelopment and copromotion of Erbitux in the United States. In 2004, the U.S. Food and Drug Administration (FDA) approved the Biologics License Application (BLA) for Erbitux for use in combination with irinotecan in the treatment of patients with Epidermal Growth Factor Receptor (EGFR)-expressing, metastatic colorectal cancer who are refractory to irinotecan-based chemotherapy and for use as a single agent in the treatment of patients with EGFR-expressing, metastatic colorectal cancer who are intolerant to irinotecan-based chemotherapy. The Company paid \$250 million in 2004 as a milestone payment for the initial approval of Erbitux. Also in 2004, the FDA approved ImClone's Chemistry, Manufacturing and Controls supplemental BLA (sBLA) for licensure of its BB36 manufacturing facility. On March 1, 2006, the FDA approved Erbitux for use in the treatment of squamous cell carcinoma of the head and neck. As a result of the FDA approval, the Company will pay a \$250 million milestone payment to ImClone by March 31, 2006. Under the agreement, ImClone receives a distribution fee based on a flat rate of 39% of product revenues in North America. In addition, the Company has the co-exclusive right to commercialize Erbitux in Japan (ImClone having previously granted co-exclusive right to Merck KGaA in Japan). In December 2004, the Company, its Japanese affiliate (BMKK), Merck KGaA, Merck Ltd., and ImClone executed a joint development agreement for Erbitux in Japan.

The Company accounts for the \$250 million approval milestone paid in 2004 and the additional \$250 million milestone expected to be paid by March 31, 2006, as license acquisitions and amortizes the payments into cost of products sold over the expected useful life of the license, which is approximately 14 years. In 2005 and 2004, the Company amortized into cost of products sold \$17 million and \$14 million, respectively. The unamortized portion of the approval payment is recorded in other intangible assets, and was \$219 million and \$236 million at December 31, 2005 and 2004, respectively.

The Company accounts for its investment in ImClone under the equity method and records its share of the results in equity in net income of affiliates in the consolidated statement of earnings. The Company's recorded investment in ImClone common stock as of December 31, 2005 and 2004 was \$66 million and \$72 million, respectively. The Company holds 14.4 million shares of ImClone stock, representing approximately 17% of ImClone's shares outstanding at December 31, 2005 and 2004. On a per share basis, the carrying value of the ImClone investment and the closing market price of the ImClone shares as of December 31, 2005 were \$4.55 and \$34.24, respectively, compared to \$5.03 and \$46.08, respectively, as of December 31, 2004.

The Company determines its equity share in ImClone's net income or loss by eliminating from ImClone's results the milestone revenue ImClone recognizes for the \$400 million in pre-approval milestone payments made by the Company from 2001 through 2003. The Company recorded \$80 million of the pre-approval milestone payments as an equity investment and expensed the remaining \$320 million as acquired in-process research and development during that period. Milestone revenue recognized by ImClone in excess of \$400 million will not be eliminated by the Company in determining its equity share in ImClone's results. For its share of ImClone's results of operations, the Company recorded a net loss of \$5 million in 2005, income of \$9 million in 2004, and a net loss of \$36 million in 2003. The Company recorded net sales for Erbitux of \$413 million in 2005 and \$261 million in 2004.

Merck

In April 2004, the Company entered into a collaboration agreement with Merck & Co., Inc. (Merck) for worldwide codevelopment and copromotion of muraglitazar, the Company's dual PPAR (peroxisome proliferator activated receptor) agonist, currently in Phase III clinical development for use in treating type 2 diabetes. Under the terms of the agreement, the Company received a \$100 million upfront payment in May 2004, and a \$55 million milestone payment in January 2005 for the submission of the New Drug Application (NDA).

In December 2004 the Company submitted an NDA to the FDA for regulatory approval of muraglitazar. In October 2005, the FDA issued an approvable letter for muraglitazar requesting additional information from ongoing clinical trials to more fully address the cardiovascular safety profile of the product. The Company, while continuing discussions with the FDA, has determined that it will likely have to initiate additional new trials to gain regulatory approval and is considering a range of options, including conducting such additional studies or terminating further development of muraglitazar. The additional studies could take approximately five years to complete. In December 2005, the Company and Merck terminated their collaboration agreement for muraglitazar with all rights returning to the Company as of December 21, 2005. As a result of the termination of the agreement, the Company recognized \$143 million of deferred income in the fourth quarter of 2005 that was recorded in "Other expense, net." The Company has a composition of matter patent that expires in the United States in 2020.

Summary Financial Information

Following is summarized financial information for the Company's equity investments in ImClone and a joint venture with Sanofi in Europe and Asia:

Dollars in Millions	2005	2004	2003
Revenues	\$ 2,819	\$ 2,427	\$ 1,605
Gross profit	2,242	1,965	794
Net income	797	673	288
Current assets	2,307	2,206	827
Non-current assets	434	371	259
Current liabilities	1,632	1,447	829
Non-current liabilities	850	949	527

Note 3 Restructuring

2005 Activities

During 2005 the Company recorded pre-tax charges of \$33 million, related to the termination benefits and other related costs for workforce reductions and downsizing and streamlining of worldwide operations primarily in North America, Latin America, Europe, Africa and Asia. Of these charges, \$31 million related to employee termination benefits and related expenses for approximately 640 selling and administrative personnel, which includes the restructuring of its U.S. cardiovascular/metabolics primary care sales organization and workforce headcount reduction, \$1 million related to retention bonuses and \$1 million related to asset impairments. These charges were offset by a \$1 million adjustment reflecting changes in estimates for restructuring actions taken in prior periods.

The following table presents a detail of the charges by segment and type. The Company expects to substantially complete these restructuring activities in 2006.

Dollars in Millions	Employees	Termination Benefits	Other Exit Costs	Relocation and Retention	Asset Write-Downs	Total
Pharmaceuticals	620	\$ 27	\$ 1	\$ 1	\$ 1	\$ 30
Nutritionals	13	1	—	—	—	1
Other Health Care	7	2	—	—	—	2
Subtotal	640	30	1	1	1	33
Changes in estimates	—	(3)	2	—	—	(1)
Restructuring as reflected in the statement of earnings	640	\$ 27	\$ 3	\$ 1	\$ 1	\$ 32

2004 Activities

During 2004, the Company recorded pre-tax restructuring and other charges of \$116 million, relating to the termination benefits and other related costs for workforce reduction and downsizing and streamlining of worldwide operations primarily in Europe, North America, Asia and Latin America. Of these charges, \$107 million primarily related to employee termination benefits and related expenses for approximately 2,000 selling, administrative and manufacturing personnel, \$1 million related primarily to asset impairments, \$6 million related to the consolidation of certain research facilities and \$2 million of retention bonuses. These charges were partially offset by an \$8 million adjustment reflecting changes in estimates for restructuring actions taken in prior periods and a \$4 million gain on the sale of a research facility previously written off as restructuring.

The following table presents a detail of the charges by segment and type. The Company has substantially completed these restructuring activities.

Dollars in Millions	Employees	Termination Benefits	Other Exit Costs	Asset Write-Downs	Relocation and Retention	Total
Pharmaceuticals	1,440	\$ 73	\$ 5	\$ 1	\$ 8	\$ 87
Other Health Care	350	18	—	—	—	18
Corporate/Other	210	11	—	—	—	11
Subtotal	2,000	102	5	1	8	116
Changes in estimates	—	(7)	—	(1)	—	(8)
Gain in sale of research facility	—	—	—	(4)	—	(4)
Restructuring as reflected in the statement of earnings	2,000	\$ 95	\$ 5	\$ (4)	\$ 8	\$ 104

2003 Activities

During 2003, the Company recorded pre-tax charges of \$65 million, relating to the termination benefits and other related costs for workforce reduction and downsizing and streamlining of worldwide operations primarily in Europe, North America, Asia and Latin America. Of these charges, \$50 million related to employee termination benefits and related expenses for approximately 950 selling, administrative and manufacturing personnel, \$13 million related to the consolidation of certain research facilities and \$2 million of retention bonuses. These charges were offset by a \$39 million adjustment reflecting changes in estimates for restructuring actions taken in prior periods, which principally is due to higher than anticipated proceeds from disposal of assets and reduced separation costs.

The following table presents a detail of the charges by segment and type. The Company has substantially completed these restructuring activities.

Dollars in Millions	Employees	Termination Benefits	Other Exit Costs	Asset Write-Downs	Relocation and Retention	Total
Pharmaceuticals	850	\$ 39	\$ 3	\$ —	\$ 15	\$ 57
Other Health Care	100	8	—	—	—	8
Subtotal	950	47	3	—	15	65
Changes in estimates	—	(7)	(3)	(29)	—	(39)
Restructuring as reflected in the statement of earnings	950	\$ 40	\$ —	\$ (29)	\$ 15	\$ 26

Rollforward

Restructuring charges and spending against liabilities associated with prior and current actions are as follows:

Dollars in Millions	Employee Termination Liability	Other Exit Cost Liability	Total
Balance at December 31, 2002	\$ 67	\$ 42	\$ 109
Charges	47	3	50
Spending	(56)	(35)	(91)
Changes in estimate	(7)	(3)	(10)
Balance at December 31, 2003	\$ 51	\$ 7	\$ 58
Charges	102	5	107
Spending	(68)	(9)	(77)
Changes in estimate	(7)	(1)	(8)
Balance at December 31, 2004	\$ 78	\$ 2	\$ 80
Charges	30	2	32
Spending	(45)	(6)	(51)
Changes in estimate	(3)	2	(1)
Balance at December 31, 2005	\$ 60	\$ —	\$ 60

These liabilities are included in accrued expenses in the consolidated balance sheet.

Note 4 Acquisitions and Divestitures

In January 2006, the Company completed the sale of its inventory, trademark, patent and intellectual property rights related to Dovonex, a treatment for psoriasis in the United States, to Warner Chilcott Company, Inc. for \$200 million in cash. In addition, the Company will receive a royalty based on 5% of net sales of Dovonex through the end of 2007. As a result of this transaction, the Company expects to recognize a pre-tax gain of approximately \$200 million (\$126 million net of tax) in the first quarter of 2006, subject to certain post-closing adjustments.

In the third quarter of 2005, the Company completed the sale of its U.S. and Canadian Consumer Medicines business and related assets (Consumer Medicines) to Novartis AG (Novartis). Under the terms of the agreement, Novartis acquired the trademarks, patents and intellectual property rights of Consumer Medicines for \$661 million in cash, including the impact of a working capital adjustment, of which \$15 million is attributable to a post-closing supply arrangement between the Company and Novartis. The related assets include the rights to the U.S. Consumer Medicines brands in Latin America, Europe, the Middle East and Africa. The results of operations of Consumer Medicines are included in the Company's consolidated statement of earnings up to the date of disposal. As a result of this transaction, the Company recorded a pre-tax gain of \$569 million (\$370 million net of tax) in the third quarter of 2005, subject to certain post-closing adjustments.

In April 2004, the Company completed the acquisition of Acordis Speciality Fibres (Acordis). The Company purchased all the stock of Acordis for \$150 million and incurred \$8 million of acquisition costs in connection with the transaction. An additional \$10 million payment is contingent on the achievement of future production volumes. The purchase price for the acquisition was allocated to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values at the acquisition date. Of the \$158 million, \$63 million was allocated to in-process research and development, which was immediately expensed, and \$22 million was assigned to identifiable intangible assets, predominantly patents. The excess of the purchase price over the estimated fair values of net assets acquired was recorded as goodwill. This acquisition was accounted for by the purchase method, and, accordingly, results of operations have been included in the accompanying consolidated financial statements from the date of acquisition.

In February 2004, the Company completed the divestiture of its Adult Nutritional business to Novartis for \$386 million, including \$20 million contingent on the achievement of contractual requirements, which were satisfied, and a \$22 million upfront payment for a supply agreement. The Company recorded a total pre-tax gain of \$320 million (\$198 million net of tax), which included the \$20 million contingent payment and a \$5 million reduction in Company goodwill associated with the Mead Johnson product lines.

Note 5 Discontinued Operations

In May 2005, the Company completed the sale of Oncology Therapeutics Network (OTN) to One Equity Partners LLC for cash proceeds of \$197 million, including the impact of a preliminary working capital adjustment. The Company recorded a pre-tax gain of \$63 million (\$13 million net of tax) that was presented as a gain on sale of discontinued operations in the consolidated statement of earnings. OTN was previously presented as a separate segment.

The following amounts related to the OTN business have been segregated from continuing operations and reported as discontinued operations through the date of disposition, and do not reflect the costs of certain services provided to OTN by the Company. Such costs, which were not allocated by the Company to OTN, were for services that included legal counsel, insurance, external audit fees, payroll processing, and certain human resource services and information technology systems support.

	Year ended December 31,		
Dollars in Millions	2005	2004	2003
Net sales	\$ 1,015	\$ 2,506	\$ 2,241
(Loss)/earnings before income taxes	(8)	15	14
Net (loss)/earnings from discontinued operations	(5)	10	9

The consolidated balance sheet at December 31, 2004, includes OTN net assets expected to be sold. These include \$332 million of assets primarily consisting of receivables and \$542 million of liabilities primarily consisting of accounts payable. In addition, goodwill related to OTN at December 31, 2004 of \$80 million was written-off against the gain on sale in the second quarter of 2005.

The consolidated statement of cash flows includes the OTN business for all periods presented through the date of disposition. The Company uses a centralized approach to the cash management and financing of its operations and accordingly, debt was not allocated to this business. Cash flows from operating activities of discontinued operations consist of outflows of \$265 million for the year ended December 31, 2005 and cash inflows of \$134 million and \$95 million for the years ended December 31, 2004 and 2003, respectively. Cash flows used in investing activities of discontinued operations were \$2 million for the year ended December 31, 2004 and there were no investing activities for the years ended December 31, 2005 and 2003.

Note 6 Earnings Per Share

The numerator for basic earnings per share is net earnings available to common stockholders. The numerator for diluted earnings per share is net earnings available to common stockholders with interest expense added back for the assumed conversion of the convertible debt into common stock. The denominator for basic earnings per share is the weighted average number of common stock outstanding during the period. The denominator for diluted earnings per share is weighted average shares outstanding adjusted for the effect of dilutive stock options and assumed conversion of the convertible debt into common stock. The computations for basic and diluted earnings per common share are as follows:

Amounts in Millions, Except Per Share Data	Year Ended December 31,		
	2005	2004	2003
Basic:			
Earnings from Continuing Operations	\$ 2,992	\$ 2,378	\$ 3,097
Discontinued Operations			
Net Earnings	(5)	10	9
Net Gain on Disposal	13	—	—
Net Earnings	\$ 3,000	\$ 2,388	\$ 3,106
Basic Earnings Per Share:			
Average Common Shares Outstanding	1,952	1,942	1,937
Earnings from Continuing Operations	\$ 1.53	\$ 1.23	\$ 1.60
Discontinued Operations			
Net Earnings	—	—	—
Net Gain on Disposal	—	—	—
Net Earnings per Common Share	\$ 1.53	\$ 1.23	\$ 1.60
Diluted:			
Earnings from Continuing Operations	\$ 2,992	\$ 2,378	\$ 3,097
Interest expense on conversion of convertible debt bonds, net of tax	22	7	1
Discontinued Operations			
Net Earnings	(5)	10	9
Net Gain on Disposal	13	—	—
Net Earnings	\$ 3,022	\$ 2,395	\$ 3,107
Diluted Earnings Per Share:			
Average Common Shares Outstanding	1,952	1,942	1,937
Conversion of convertible debt bonds	29	29	7
Incremental shares outstanding assuming the exercise of dilutive stock options	2	5	6
	1,983	1,976	1,950
Earnings from Continuing Operations	\$ 1.52	\$ 1.21	\$ 1.59
Discontinued Operations			
Net Earnings	—	—	—
Net Gain on Disposal	—	—	—
Net Earnings per Common Share	\$ 1.52	\$ 1.21	\$ 1.59

Weighted-average shares issuable upon the exercise of stock options, which were not included in the diluted earnings per share calculation or because they were not dilutive, were 156 million in 2005, 126 million in 2004, and 114 million in 2003.

Note 7 Other Expense, Net

The components of other expense, net are:

	Year Ended December 31,		
Dollars in Millions	2005	2004	2003
Interest expense	\$ 349	\$ 310	\$ 277
Interest income	(148)	(105)	(65)
Foreign exchange transaction losses	58	5	23
Other, net	(222)	(158)	(56)
Other expense, net	\$ 37	\$ 52	\$ 179

In 2005, 2004 and 2003 interest expense was reduced by net interest swap gains of \$52 million, \$151 million and \$116 million, respectively. Interest income relates primarily to cash, cash equivalents and investments in marketable securities. Other, net includes income from third-party contract manufacturing, royalty income and expense, deferred income recognized from the termination of the collaborative agreement for muraglitazar, gains and losses on disposal of investments and property, plant and equipment and debt retirement costs.

Note 8 Income Taxes

The components of earnings (loss) from continuing operations before minority interest and income taxes were:

	Year Ended December 31,		
Dollars in Millions	2005	2004	2003
U.S.	\$ 809	\$ 478	\$ 899
Non-U.S.	3,707	3,940	3,781
	\$ 4,516	\$ 4,418	\$ 4,680

The above amounts are categorized based on the location of the taxing authorities.

The provision/(benefit) for income taxes attributable to continuing operations consisted of:

	Year Ended December 31,		
Dollars in Millions	2005	2004	2003
Current:			
U.S.	\$ 1,058	\$ 513	\$ 423
Non-U.S.	686	728	538
	1,744	1,241	961
Deferred:			
U.S.	(852)	264	232
Non-U.S.	40	14	17
	(812)	278	249
	\$ 932	\$ 1,519	\$ 1,210

The Company's provision for income taxes in 2005, 2004 and 2003 was different from the amount computed by applying the statutory U.S. federal income tax rate to earnings from continuing operations before minority interest and income taxes, as a result of the following:

	% of Earnings Before Minority Interest and Income Taxes						
Dollars in Millions	2005		2004		2003		
Earnings from Continuing Operations Before Minority Interest and Income Taxes	\$ 4,516		\$ 4,418		\$ 4,680		
U.S. statutory rate	1,581	35.0%	1,546	35.0%	1,638	35.0%	
Effect of operations in Ireland, Puerto Rico and Switzerland	(708)	(15.7)%	(660)	(14.9)%	(734)	(15.7)%	
State and local taxes (net of valuation allowance)	2	0.1%	(14)	(0.3)%	14	0.3%	
Changes in estimate for contingent tax matters	114	2.5%	293	6.6%	197	4.2%	
Non-deductible reserves	—	—	12	0.3%	88	1.9%	
Anticipated dividend repatriation under AJCA	(135)	(3.0)%	575	13.0%	—	—	
Federal and foreign valuation allowance	32	0.7%	142	3.2%	133	2.8%	
Foreign and other	46	1.0%	(375)	(8.5)%	(126)	(2.7)%	
	\$ 932	20.6%	\$ 1,519	34.4%	\$ 1,210	25.8%	

The effective income tax rate on earnings from continuing operations before minority interest and income taxes was 20.6% in 2005 compared with 34.4% in 2004 and 25.8% in 2003. The lower effective tax rate in 2005 was due primarily to a 2004 charge of approximately \$575 million for estimated deferred income taxes related to the repatriation of approximately \$9 billion in special dividends from the Company's non-U.S. subsidiaries pursuant to the American Jobs Creation Act (AJCA), a 2004 charge related to the establishment of a valuation allowance against certain charitable contributions, a tax benefit in 2005 associated with the release of certain tax contingency reserves resulting from the settlement of examinations by the Internal Revenue Service (IRS) for the years 1998 through 2001, and a change in estimate in 2005 related to the reduction of the aforementioned 2004 AJCA deferred tax charge, partially offset by lower estimated foreign tax credits in 2005. The increase in the 2004 effective tax rate over the 2003 effective tax rate was primarily attributable to the aforementioned 2004 AJCA deferred tax charge of \$575 million, the aforementioned establishment of a valuation allowance against certain charitable contributions in 2004, an increase in estimates for contingent tax matters, partially offset by the favorable resolution of certain tax refund claims, increased foreign tax credits, and in 2003, the effect of certain litigation reserves as non-deductible.

In the fourth quarter of 2004, the Company disclosed that it anticipated repatriating approximately \$9 billion in special dividends in 2005 and recorded a \$575 million provision for deferred taxes pursuant to the AJCA as enacted and other pending matters. The Company repatriated approximately \$6.2 billion from foreign subsidiaries in the first quarter of 2005 and repatriated the remaining balance of approximately \$2.8 billion in the fourth quarter of 2005. The Company expects that approximately all of the \$9 billion repatriated in 2005 will qualify as special dividends subject to finalization of its 2005 U.S. federal income tax return and any related tax examinations by the IRS. The Company has used and expects to continue to use the special dividends in accordance with requirements established by the AJCA and the U.S. Treasury Department. During the second quarter of 2005, the U.S. Treasury Department issued AJCA related guidance clarifying that the "gross-up" for foreign taxes associated with the special dividends also qualifies for the 5.25% tax rate established by the AJCA. As a result of this guidance, the Company reduced the \$575 million provision by recording a benefit of approximately \$135 million in its tax provision for 2005.

The components of current and non-current deferred income tax assets (liabilities) were:

	December 31,	
Dollars in Millions	2005	2004
Acquired in-process research and development	\$ 976	\$ 1,156
Intercompany profit and other inventory items	225	274
Foreign tax credit carryforward	975	801
Deferred income	136	194
Alternative minimum tax and research and development credit carryforward	125	89
Charitable contribution carryforward	117	135
State tax net operating loss carryforward	306	194
Foreign deferred tax assets	252	305
Postretirement and pension benefits	(223)	(213)
Depreciation	(245)	(332)
Deferred foreign currency gain/loss	(3)	120
Anticipated dividend repatriation under AJCA	—	(575)
Legal settlements	127	92
Other, net	171	(20)
	2,939	2,220
Valuation allowance	(559)	(507)
Deferred tax assets, net	\$ 2,380	\$ 1,713
Recognized as:		
Deferred Income Taxes – Current	\$ 776	\$ 805
Deferred Income Taxes – Non-Current	1,808	1,129
U.S. and Foreign Income Taxes Payable	(26)	(18)
Other Liabilities – Non-Current	(178)	(203)
Total	\$ 2,380	\$ 1,713

The valuation allowance of \$559 million at December 31, 2005 relates to \$79 million of foreign and state net deferred tax assets, \$363 million of foreign and state net operating loss and tax credit carryforwards, and \$117 million of charitable contribution carryforwards that the Company currently believes are not likely to be realized.

The Company has recorded deferred tax assets related to U.S. foreign tax credit carryforwards of approximately \$975 million and U.S. research tax credit carryforwards of approximately \$120 million, which expire in varying amounts beginning in 2012. Realization of the foreign tax credit and research tax credit carryforwards is dependent on generating sufficient domestic-sourced taxable income prior to their expiration. Although realization is not assured, management believes it is more likely than not that these deferred tax assets will be realized. The Company anticipates increasing its level of domestic profitability over time by undertaking actions such as increasing its biologics manufacturing capacity in the U.S. While increasing domestic profitability will likely cause the Company's effective tax rate to increase, it will also further enhance the Company's ability to utilize its foreign tax credit and research tax credit carryforwards. The amount of foreign tax credit and research tax credit carryforwards considered realizable, however, could be reduced in the near term if the outcome of the Plavix litigation in the U.S. is unfavorable, and/or if the timing of generic competition for Plavix were to be accelerated. If such events occur, the Company may need to record significant additional valuation allowances against these deferred tax assets. For additional information on Plavix litigation, see Note 20 "Legal Proceedings and Contingencies."

Income taxes paid during the year were \$1,556 million, \$822 million and \$869 million in 2005, 2004 and 2003, respectively.

The current tax benefit realized upon the exercise of stock options is charged to capital in excess of par value of stock and amounted to \$19 million, \$26 million and \$10 million in 2005, 2004 and 2003, respectively.

As of December 31, 2005, the Company had approximately \$8.4 billion of undistributed earnings of foreign subsidiaries for which taxes have not been provided as the Company has invested or expects to invest these undistributed earnings permanently offshore. If in the future these earnings are repatriated to the United States, or if the Company determines such earnings will be remitted in the foreseeable future, additional tax provisions would be required. Due to complexities in the tax laws and the assumptions that would have to be made, it is not practicable to estimate the amounts of income taxes that would have to be provided.

The Company has settled its U.S. federal income tax returns with the Internal Revenue Service (IRS) through 2001. The Company's U.S. Federal income tax returns for 2002 and 2003 are currently under examination by the IRS. The Company conducts business in various states, municipalities, and foreign countries through its subsidiary companies. State, local and foreign tax authorities routinely examine the Company's income tax returns.

The Company establishes liabilities for possible assessments by taxing authorities resulting from known tax exposures including, but not limited to, transfer pricing, certain tax credits, deductibility of certain expenses and various state, local, and foreign tax matters. Such amounts represent a reasonable provision for taxes ultimately expected to be paid, and may need to be adjusted over time as more information becomes known. The effect of changes in estimates related to contingent tax matters is included in the effective tax rate reconciliation above. In 2005, the Company recognized an income tax benefit of approximately \$159 million due to the settlement of the Company's U.S. Federal income tax returns for the years 1998 through 2001.

In 2002, the Company reorganized the structure of its ownership of many of its non-U.S. subsidiaries. The principal purpose of the reorganization was to facilitate the Company's ability to efficiently deploy its financial resources outside the United States. The Company believes that the reorganization transactions were generally tax-free both inside and outside the United States. It is possible, however, that taxing authorities in particular jurisdictions could assert tax liabilities arising from the reorganization transactions or the operations of the reorganized subsidiaries. It is not reasonably possible to predict whether any taxing authority will assert such a tax liability or to reasonably estimate the possible loss or range of loss with respect to any such asserted tax liability. The Company would vigorously challenge any such assertion and believes that it would prevail but there can be no assurance of such a result. If the Company were not to prevail in final, non-appealable determinations, it is possible the impact could be material.

Note 9 Receivables

The major categories of receivables follow:

	December 31,	
Dollars in Millions	2005	2004
Trade receivables	\$ 2,797	\$ 3,393
Miscellaneous receivables	788	1,201
	3,585	4,594
Less allowances	207	221
Receivables, net	\$ 3,378	\$ 4,373

Note 10 Inventories

The major categories of inventories follow:

	December 31,	
Dollars in Millions	2005	2004
Finished goods	\$ 867	\$ 1,004
Work in process	679	393
Raw and packaging materials	514	433
Inventories, net	\$ 2,060	\$ 1,830

The Company has finished good inventories that could be impaired if it is determined that such inventories cannot be reworked for commercialization. As of December 31, 2005, the carrying value of these inventories was \$25 million and no allowance has been provided.

Note 11 Property, Plant and Equipment

The major categories of property, plant and equipment follow:

	December 31,	
Dollars in Millions	2005	2004
Land	\$ 280	\$ 290
Buildings	4,560	4,497
Machinery, equipment and fixtures	4,574	4,686
Construction in progress	570	536
	9,984	10,009
Less accumulated depreciation	4,291	4,244
Property, plant and equipment, net	\$ 5,693	\$ 5,765

Capitalized interest is included in the categories of property, plant and equipment shown above. The Company capitalized interest of \$9 million, \$10 million and \$35 million in the years ended December 31, 2005, 2004 and 2003, respectively.

Note 12 Goodwill

The changes in the carrying amount of goodwill for the years ended December 31, 2005 and 2004 were as follows:

Dollars in Millions	Pharmaceuticals Segment	Nutritionals Segment	Other Health Care Segment	Discontinued Operations	Total
Balance as of December 31, 2003	\$ 4,448	\$ 118	\$ 190	\$ 80	\$ 4,836
Purchase accounting adjustments:					
Reduction due to sale of Adult Nutritional business	—	(5)	—	—	(5)
Purchase price and allocation adjustments	—	—	74	—	74
Balance as of December 31, 2004	\$ 4,448	\$ 113	\$ 264	\$ 80	\$ 4,905
Purchase accounting adjustment:					
Reduction due to sale of OTN	—	—	—	(80)	(80)
Reduction due to sale of Consumer Medicines	—	—	(1)	—	(1)
Purchase price and allocation adjustments	—	—	(1)	—	(1)
Balance as of December 31, 2005	\$ 4,448	\$ 113	\$ 262	\$ —	\$ 4,823

Note 13 Other Intangible Assets

As of December 31, 2005 and 2004, other intangible assets consisted of the following:

	December 31,	
Dollars in Millions	2005	2004
Patents/Trademarks	\$ 269	\$ 278
Less accumulated amortization	113	90
Patents/Trademarks, net	156	188
Licenses	431	523
Less accumulated amortization	113	116
Licenses, net	318	407
Technology	1,787	1,787
Less accumulated amortization	676	516
Technology, net	1,111	1,271
Capitalized Software	761	710
Less accumulated amortization	425	316
Capitalized Software, net	336	394
Total other intangible assets, net	\$ 1,921	\$ 2,260

In 2005, the Company recorded impairment charges of \$42 million resulting from actual and estimated future sales declines of *Tequin*.

Amortization expense for other intangible assets for the years ended December 31, 2005, 2004 and 2003 was \$352 million, \$316 million and \$298 million, respectively.

Expected amortization expense related to the current net carrying amount of other intangible assets follows:

Years Ending December 31,	Dollars in Millions
2006	\$ 351
2007	331
2008	276
2009	241
2010	213
Later Years	509

Note 14 Short-Term Borrowings And Long-Term Debt

Short-term borrowings at the end of 2005 and 2004 were \$231 million and \$1,883 million, respectively, with the reduction of these borrowings due primarily to the retirement of commercial paper.

In August 2005 a wholly-owned subsidiary of the Company entered into a new \$2.5 billion term facility with a syndicate of bank lenders. Borrowings under this facility are guaranteed by the Company, the subsidiaries of the borrower and by certain European subsidiaries of the Company. This facility contains a five-year tranche of up to \$2.0 billion and a two-year tranche of up to \$500 million. Interest is paid on a periodic basis, as agreed with the lenders, at an annual rate equal to the applicable LIBOR plus 0.25%. The Company is subject to substantially the same covenants as those included in its December 2004 Revolving Credit facility. The Company is also subject to further restrictions, including certain financial covenants. Prior to borrowing any proceeds against this facility, the Company obtained a waiver from the lenders for a covenant default under this facility due to a one-time intercompany distribution. As of December 31, 2005, this facility was fully drawn and the Company was in full compliance with all covenants.

During the second quarter of 2005, the Company repurchased all of its outstanding \$2.5 billion aggregate principal amount 4.75% Notes due 2006, and incurred an aggregate pre-tax loss of approximately \$69 million in connection with the early redemption of the Notes and termination of related interest rate swaps.

In December 2004, the Company replaced its prior \$1 billion revolving credit facilities with a new \$2 billion five year revolving credit facility from a syndicate of lenders, which is extendable on the anniversary date with the consent of the lenders. This facility contains a financial covenant whereby the ratio of consolidated debt to consolidated capital cannot exceed 50%. The Company has been in compliance with this covenant since the inception of the new facility. There were no borrowings outstanding under the revolving credit facilities at December 31, 2005 and 2004. The Company has unused short-term lines of credit with foreign banks of \$198 million and \$158 million at December 31, 2005 and 2004, respectively.

The components of long-term debt were as follows:

	December 31,	
Dollars in Millions	2005	2004
4.75% Notes, due 2006	\$ —	\$ 2,507
5.75% Notes, due 2011	2,425	2,488
Floating Rate Bank Term Facility, due 2010	2,000	—
Floating Rate Convertible Debentures, due 2023 ⁽¹⁾	1,188	1,183
5.25% Notes, due 2013	593	610
Floating Rate Bank Term Facility, due 2007	500	—
4.00% Notes, due 2008	387	396
6.80% Debentures, due 2026	384	367
7.15% Debentures, due 2023	365	365
6.88% Debentures, due 2097	296	296
1.10% Yen Notes, due 2008	106	120
5.75% Industrial Revenue Bonds, due 2024	34	34
1.43% Yen Notes, due 2008	30	34
1.81% Yen Notes, due 2010	30	34
Variable Rate Industrial Revenue Bonds, due 2030	15	15
Other	11	14
	\$ 8,364	\$ 8,463

⁽¹⁾ The Company's outstanding \$1.2 billion of convertible debentures pay interest quarterly at an annual rate equal to 3-month LIBOR, reset quarterly, minus 0.50% (the yield never to be less than zero) and have a final maturity of September 15, 2023. The debentures are callable at par at any time on or after September 21, 2008 by the issuer. Holders can also redeem some or all of their debentures at par on September 15, 2008, 2013, and 2018, or if a fundamental change in ownership of the Company occurs. The bond has an initial conversion price of \$41.28, or a conversion rate of 24.2248 shares, which will be adjustable depending on the average closing prices for the applicable period. The maximum conversion rate is 38.7597 shares.

The Company has entered into fixed to floating interest rate swaps for \$3.4 billion of its long-term debt. During 2004, 2003 and 2002 the Company executed several fixed to floating interest rate swaps to convert \$6.2 billion of the Company's fixed rate debt to be paid in 2006, 2008, 2011, 2013, 2023 and 2026 to variable rate debt. For the year ended December 31, 2005, the Company recognized a net reduction in interest expense of \$54 million that reflects the benefit of the lower floating rate obtained in the swap agreement. In April 2005, in connection with the early redemption of its \$2.5 billion Notes due 2006, the Company terminated \$2 billion notional amount of its 2006 fixed-to-floating interest rate swap agreements and incurred a pre-tax loss of \$28 million. In June 2005, the Company terminated \$500 million notional amount of its 2011 fixed-to-floating interest rate swap agreements related to its \$2.5 billion Notes due 2011, and incurred a pre-tax loss of \$23 million. This loss will be amortized to interest expense over the remaining life of the Notes, due 2011, of which \$2 million was recognized in 2005. In September 2005, the Company terminated \$350 million notional amount of its 2026 fixed-to-floating interest rate swap agreements related to its \$350 million Debentures due 2026 and received a gain of \$39 million. This gain will be recognized against interest expense over the remaining life of the Debentures due 2026, of which approximately \$1 million was recognized in 2005. Cash payments for interest, including payments due to interest rate swaps, were \$598 million, \$354 million and \$290 million in 2005, 2004 and 2003, respectively. The Company's cash receipts from interest rate swaps were \$275 million, \$298 million and \$166 million in 2005, 2004 and 2003, respectively, and were excluded from cash payments for interest.

	Payments due by period						
Dollars in Millions	Total	2006	2007	2008	2009	2010	Later Years
Long-Term Debt ⁽²⁾	\$ 8,364	\$ —	\$ 504	\$ 1,715	\$ 3	\$ 2,030	\$ 4,112

⁽²⁾ 2006 obligations are included in short-term borrowings on the Company's consolidated balance sheet at December 31, 2005 and all balances approximate the outstanding nominal long-term debt values. The Company's convertible debenture is included as due for payment in 2008, as it contains a 2008 put and call feature as described above.

At December 31, 2005, the Company had provided financial guarantees in the form of stand-by letters of credit and performance bonds. The majority of the stand-by letters of credit are with insurance companies in support of third-party liability programs. The performance bonds relate to the sale of Company product to various foreign ministries of health in the Middle East. The Company believes the significant majority of these guarantees will expire without being funded. The amounts of these obligations are presented in the following table:

Dollars in Millions	Expiration Period			
	Total	Less than 1 year	1 to 2 years	Greater than 2 years
Stand-by letters of credit	\$ 66	\$ 26	\$ 40	\$ —
Performance bonds and guarantees	8	6	—	2
Total other commercial commitments	\$ 74	\$ 32	\$ 40	\$ 2

Note 15 Stockholders' Equity

Changes in common shares, treasury stock, capital in excess of par value of stock, and restricted stock were:

Dollars and Shares in Millions	Common Shares Issued	Treasury Shares	Cost of Treasury Stock	Capital in Excess of Par Value of Stock	Restricted Stock
Balance at December 31, 2002	2,201	264	\$ (11,502)	\$ 2,491	\$ (52)
Issued pursuant to stock plans and options	—	(3)	64	(14)	(23)
Amortization of restricted stock	—	—	—	—	18
Lapses and forfeitures of restricted stock	—	—	(2)	—	2
Balance at December 31, 2003	2,201	261	(11,440)	2,477	(55)
Issued pursuant to stock plans and options	1	(6)	137	12	(32)
Amortization of restricted stock	—	—	—	—	24
Lapses and forfeitures of restricted stock	—	—	(8)	2	6
Balance at December 31, 2004	2,202	255	(11,311)	2,491	(57)
Issued pursuant to stock plans and options	3	(7)	148	36	(40)
Amortization of restricted stock	—	—	—	—	22
Lapses and forfeitures of restricted stock	—	—	(5)	1	4
Balance at December 31, 2005	2,205	248	\$ (11,168)	\$ 2,528	\$ (71)

Each share of the Company's preferred stock is convertible into 16.96 shares of common stock and is callable at the Company's option. The reductions in the number of issued shares of preferred stock in 2005, 2004, and 2003 were due to conversions into shares of common stock.

Dividends declared per common share were \$1.12 in 2005, \$1.12 in 2004 and \$1.12 in 2003.

The accumulated balances related to each component of other comprehensive income/(loss) were as follows:

Dollars in Millions	Foreign Currency Translation	Deferred (Income)/Loss on Effective Hedges	Minimum Pension Liability Adjustment	Available for Sale Securities	Accumulated Other Comprehensive Income/(Loss)
Balance at December 31, 2002	\$ (724)	\$ (87)	\$ (94)	\$ 1	\$ (904)
Other comprehensive income/(loss)	233	(171)	(36)	23	49
Balance at December 31, 2003	(491)	(258)	(130)	24	(855)
Other comprehensive income/(loss)	208	(51)	(93)	(1)	63
Balance at December 31, 2004	(283)	(309)	(223)	23	(792)
Other comprehensive income/(loss)	(270)	325	(6)	(22)	27
Balance at December 31, 2005	\$ (553)	\$ 16	\$ (229)	\$ 1	\$ (765)

Stock Compensation Plans

Under the Company's 2002 Stock Incentive Plan, executive officers and key employees may be granted options to purchase the Company's common stock at no less than 100% of the market price on the date the option is granted. Options generally become exercisable in installments of 25% per year on each of the first through the fourth anniversaries of the grant date and have a maximum term of 10 years. Additionally, the plan provides for the granting of stock appreciation rights whereby the grantee may surrender exercisable rights and receive common stock and/or cash measured by the excess of the market price of the common stock over the option exercise price.

Under the terms of the 2002 Stock Incentive Plan, authorized shares include 0.9% of the outstanding shares per year through 2007, as well as the number of shares tendered in a prior year to pay the purchase price of options and the number of shares previously utilized to satisfy withholding tax obligations upon exercise. Shares which were available for grant in a prior year but were not granted in such year and shares which were cancelled, forfeited or expired are also available for future grant.

The 2002 Stock Incentive Plan provides for the granting of common stock to key employees, subject to restrictions as to continuous employment. Restrictions generally expire over a five-year period from date of grant. Compensation expense is recognized over the restricted period. At December 31, 2005 and 2004, there were 4.2 million and 2.9 million shares of restricted stock outstanding under the plan, respectively. In 2005, 1.8 million shares of restricted stock were granted with a fair value of \$24.61 per common share.

The 2002 Stock Incentive Plan also incorporates the Company's long-term performance awards. These awards, which are delivered in the form of a target number of performance shares, have a three-year cycle. For 2004 to 2006, the awards will be based 50% on cumulative EPS, 50% on cumulative sales, with the ultimate payout modified by the Company's total stockholder return versus the 11 companies in its proxy peer group. If threshold targets are not met for the performance period, no payment will be made under the long-term performance award plan. Maximum performance for all three measures will result in a maximum payout of 253% of target. At December 31, 2005 and 2004, there were 1.8 million and 0.9 million performance shares outstanding under the plan, respectively. In 2005, 1.1 million performance shares were granted with a fair value of \$25.45 per common share.

Under the TeamShare Stock Option Plan, full-time employees, excluding key executives, were granted options to purchase the Company's common stock at the market price on the date the options were granted. The Company authorized 66 million shares for issuance under the plan. Individual grants generally became exercisable evenly on the third, fourth, and fifth anniversary of the grant date and have a maximum term of 10 years. Options on 35.3 million shares have been exercised under the plan as of December 31, 2005.

The fair value of the options granted during 2005, 2004 and 2003 was estimated as \$5.49 per common share, \$5.91 per common share and \$5.15 per common share, respectively, on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	2005	2004	2003
Dividend yield	4.6%	4.4%	4.0%
Volatility	29.4%	30.0%	29.7%
Risk-free interest rate	4.4%	3.5%	3.5%
Expected life (years)	7	7	7

Stock option transactions were:

Shares in Millions	Shares of Common Stock		Weighted Average Exercise Price of Shares
	Available for Option Award	Issued Under Plan	
Balance at December 31, 2002	26	149	\$ 41.20
Authorized	19	—	—
Granted	(22)	22	23.19
Exercised	—	(4)	13.76
Lapsed	6	(6)	43.62
Balance at December 31, 2003	29	161	\$ 39.24
Authorized	18	—	—
Granted	(20)	20	27.88
Exercised	—	(7)	14.56
Lapsed	11	(11)	40.69
Balance at December 31, 2004	38	163	\$ 38.87
Authorized	18	—	—
Granted	(20)	20	25.37
Exercised	—	(9)	16.26
Lapsed	10	(10)	37.67
Balance at December 31, 2005	46	164	\$ 38.45

The following tables summarize information concerning the Company's stock compensation plans and currently outstanding and exercisable options:

Shares in Millions	Number of securities to be issued upon exercise of outstanding options and rights (a)	Weighted average exercise price of outstanding options and rights (b)	Number of securities remaining available for future issuance under equity compensation plans excluding securities reflected in column (a) (c)
Plan Category			
Equity compensation plans approved by security holders	142	\$ 37.93	36
Equity compensation plans not approved by security holders	22	41.76	10
	<u>164</u>	<u>\$ 38.45</u>	<u>46</u>

Shares in Millions	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted Average Remaining Contractual Life ⁽¹⁾	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
Range of Exercise Prices					
\$20 — \$30	81	6.83	25.73	37	25.44
\$30 — \$40	9	1.19	32.35	9	32.35
\$40 — \$50	42	3.83	47.03	39	46.96
\$50 — \$60	14	4.99	58.13	12	58.16
\$60 and up	18	3.49	63.32	16	63.32
	<u>164</u>	<u>5.24</u>	<u>\$ 38.45</u>	<u>113</u>	<u>\$ 42.23</u>

⁽¹⁾ Average contractual life remaining, in years.

At December 31, 2005, 298 million shares of common stock were reserved for issuance pursuant to stock plans, options and conversions of preferred stock. Options related to discontinued operations included in the above amounts are not material.

Note 16 Financial Instruments

The Company is exposed to market risk due to changes in currency exchange rates and interest rates. To reduce that risk, the Company enters into certain derivative financial instruments, when available on a cost-effective basis, to hedge its underlying economic exposure. These instruments are managed on a consolidated basis to efficiently net exposures and thus take advantage of any natural offsets. Derivative financial instruments are not used for speculative purposes.

The Company's primary foreign currency exposures on anticipated transactions, primarily intercompany inventory purchases expected to occur within the next two years, are the euro, Canadian dollar, Japanese yen, Mexican peso and Chinese yuan. The Company utilizes foreign currency forward contracts to hedge exposures on certain foreign currencies and designates these derivative instruments as cash flow hedges. The notional amounts of the Company's foreign exchange derivative contracts at December 31, 2005 and 2004, were \$2,296 million and \$3,461 million, respectively. For these derivatives, in which the majority qualify as hedges of future anticipated cash flows, the effective portion of changes in fair value is temporarily deferred in other comprehensive income (OCI) and then recognized in earnings when the hedged item affects earnings.

SFAS No.133 requires that the Company perform periodic assessments of hedge effectiveness. These assessments determine whether derivatives designated as qualifying hedges continue to be highly effective in offsetting changes in the cash flows of hedged items. Any ineffective portion of fair value can no longer be deferred in OCI and is included in current period earnings. For the years ended December 31, 2005 and 2004, the hedge ineffectiveness on earnings were not significant. Additionally, the Company uses foreign exchange forward contracts to offset its exposure to certain currency assets and liabilities. These foreign exchange forward contracts are not designated as hedges and, therefore, changes in the fair value of these derivatives are recognized in earnings as they occur. In 2005 and 2004, the amounts recognized in earnings related to foreign exchange forward contracts that did not qualify for hedge accounting treatment were not significant.

The fair value of option and forward contracts were assets of \$53 million and liabilities of \$362 million, at December 31, 2005 and 2004, respectively, and was recorded in other assets and accrued liabilities at December 31, 2005 and 2004, respectively. The fair value of all foreign exchange contracts is based on year-end currency rates (and the Black-Scholes model in the case of option contracts).

The Company had exposures to net foreign currency denominated assets and liabilities of approximately \$2,488 million and \$2,264 million at December 31, 2005 and 2004, respectively, primarily in Europe, Japan, Mexico, Australia and Canada.

In addition to the foreign exchange hedge contracts noted above, the Company utilizes forward contracts to hedge foreign currency denominated monetary assets and liabilities. The primary objective of these forward contracts is to protect the U.S. dollar value of foreign currency denominated monetary assets and liabilities from the effects of volatility in foreign exchange rates that might occur prior to their receipt or settlement in U.S. dollars. These foreign currency denominated monetary assets and liabilities are primarily denominated in Japanese yen and euro. The forward contracts are not designated as hedges and are marked to market through other income/expense. The notional and fair value amount of purchased foreign exchange forward contracts was \$142 million and a \$2 million liability, respectively, at December 31, 2005, and was \$229 million and a \$10 million liability, respectively, at December 31, 2004. The notional and fair value amount of sold foreign exchange forward contracts was \$47 million and a \$1 million asset, respectively, at December 31, 2005, and was \$96 million and a \$4 million asset, respectively, at December 31, 2004.

The Company also uses non U.S. dollar borrowings and, to a lesser extent, forward contracts, to hedge the foreign currency exposures of the Company's net investment in certain foreign affiliates. These non U.S. dollar borrowings and forward contracts are designated as hedges of net investments. The effective portion of foreign exchange gains or losses on these hedges is recorded as part of the foreign currency translation component of other comprehensive income. At December 31, 2005 and 2004, \$12 million in after tax gains and \$6 million in after tax losses, respectively, were recorded in the foreign currency translation component of other comprehensive income.

The Company uses derivative instruments as part of its interest rate risk management strategy. The derivative instruments used comprised principally of fixed to floating rate interest rate swaps, which are subject to fair-value hedge accounting treatment. During, 2004, 2003 and 2002, the Company executed several fixed-to-floating interest rate swap contracts with several financial institutions to convert \$6.2 billion of the Company's fixed rate debt to be paid in 2006, 2008, 2011, 2013, 2023 and 2026 to variable rate debt. The notional amounts of these swaps were \$3.4 billion and \$6.2 billion as of December 31, 2005 and 2004, respectively. In accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, the Company recognized a net reduction in interest expense of \$54 million, \$151 million and \$116 million in 2005, 2004 and 2003, respectively, that reflects the benefit of the lower floating rate obtained in the swap as compared to the fixed rate of the underlying debt. In April 2005, in connection with the early redemption of its \$2.5 billion Notes due 2006, the Company terminated \$2 billion notional amount of its 2006 fixed-to-floating interest rate swap agreements and incurred a pre-tax loss of \$28 million. In June 2005, the Company terminated \$500 million notional amount of its 2011 fixed-to-floating interest rate swap agreements related to its \$2.5 billion Notes due 2011, and incurred a pre-tax loss of \$23 million. This loss will be amortized to interest expense over the remaining life of the Notes, due 2011, of which \$2 million was recognized in 2005. In September 2005, the Company terminated \$350 million notional amount of its 2026 fixed-to-floating interest rate swap agreements related to its \$350 million Debentures due 2026 and resulted in a gain of \$39 million. This gain will be recognized against the interest expense over the remaining life of the Debentures due 2026, of which approximately \$1 million was recognized in 2005.

The swap contracts as well as the underlying debt being hedged are recorded at fair value, which resulted in an increase in non-current assets of \$21 million, current liabilities of \$51 million and a reduction in long-term debt of \$30 million, and an increase in non-current assets of \$76 million, current liabilities of \$1 million and long-term debt of \$75 million at December 31, 2005 and 2004, respectively. Swap contracts are generally held to maturity and the Company does not use derivative financial instruments for speculative purposes.

During 2005, 2004 and 2003, the Company reclassified deferred losses of \$130 million, \$234 million and \$223 million, respectively, from OCI to earnings, the majority of which was classified as cost of products sold.

The carrying amount of the Company's other financial instruments, which includes cash, cash equivalents, marketable securities, accounts receivable and accounts payable, approximates their fair value at December 31, 2005 and 2004. For long-term debt the difference between the fair value and carrying value is not material.

Note 17 Segment Information

The Company is organized in three reportable segments—Pharmaceuticals, Nutritionals and Other Health Care. The Pharmaceuticals segment is comprised of the global pharmaceutical and international consumer medicines businesses. The Nutritionals segment consists of Mead Johnson, primarily an infant formula business and children's nutritional business. The Other Health Care segment consists of ConvaTec, Medical Imaging and Consumer Medicines (United States and Canada). In the third quarter of 2005, the Company completed the sale of its Consumer Medicines business. For additional information on the sale of Consumer Medicines, see Note 4 "Acquisitions and Divestitures."

The Company's products are sold principally to the wholesale and retail trade, both nationally and internationally. Certain products are also sold to other drug manufacturers, hospitals, clinics, government agencies and the medical profession. Three wholesalers accounted for approximately 20%, 19% and 11%, respectively, of the Company's total net sales in 2005. In 2004, sales to these wholesalers accounted for 19%, 17% and 10%, respectively, of the Company's total net sales. In 2003, the same three wholesalers each accounted for approximately 17%, 15% and 13%, respectively, of the Company's total net sales. These sales were concentrated in the Pharmaceuticals segment.

Business Segments

	Net Sales			Earnings Before Minority Interest and Income Taxes			Year-end Assets	
	2005	2004	2003	2005	2004	2003	2005	2004
Dollars in Millions								
Pharmaceuticals	\$ 15,254	\$ 15,564	\$ 15,025	\$ 3,698	\$ 4,301	\$ 4,414	\$ 11,671	\$ 12,436
Nutritionals	2,205	2,001	2,023	648	586	542	1,088	1,055
Other Health Care	1,748	1,815	1,605	492	529	363	1,180	1,368
Total segments	19,207	19,380	18,653	4,838	5,416	5,319	13,939	14,859
Corporate/Other	—	—	—	(322)	(998)	(639)	14,199	15,576
Total	\$ 19,207	\$ 19,380	\$ 18,653	\$ 4,516	\$ 4,418	\$ 4,680	\$ 28,138	\$ 30,435

Corporate/Other consists principally of interest income, interest expense, certain administrative expenses and allocations to the business segments of certain corporate programs and the gain on the sale of Consumer Medicines business. Corporate/Other assets include cash and cash equivalents, marketable securities, goodwill, assets of OTN held available for sale at December 31, 2004 and sold in 2005 and certain other assets.

	Capital Expenditures			Depreciation		
	2005	2004	2003	2005	2004	2003
Dollars in Millions						
Pharmaceuticals	\$ 554	\$ 455	\$ 678	\$ 477	\$ 474	\$ 391
Nutritionals	65	55	50	38	48	39
Other Health Care	30	27	23	25	22	19
Total segments	649	537	751	540	544	449
Corporate/Other	44	49	74	37	49	42
Total	\$ 693	\$ 586	\$ 825	\$ 577	\$ 593	\$ 491

Geographic Areas

Dollars in Millions	Net Sales			Year-end Assets	
	2005	2004	2003	2005	2004
United States	\$ 10,461	\$ 10,613	\$ 10,656	\$ 20,579	\$ 15,727
Europe, Middle East and Africa	5,136	5,470	4,985	4,779	5,920
Other Western Hemisphere	1,592	1,425	1,333	1,556	7,228
Pacific	2,018	1,872	1,679	1,224	1,560
Total	\$ 19,207	\$ 19,380	\$ 18,653	\$ 28,138	\$ 30,435

The change in year-end assets in the United States and Other Western Hemisphere in 2005 from 2004 is primarily related to the 2005 cash repatriation from the Company's non-U.S. subsidiaries pursuant to the AJCA of 2004.

Note 18 Leases

Minimum rental commitments under all non-cancelable operating leases, primarily real estate and motor vehicles, in effect at December 31, 2005, were:

Years Ending December 31,	Dollars in Millions
2006	\$ 129
2007	105
2008	81
2009	58
2010	34
Later years	68
Total minimum payments	475
Less total minimum sublease rentals	63
Net minimum rental commitments	\$ 412

Operating lease rental expense (net of sublease rental income of \$15 million in 2005, \$13 million in 2004 and \$11 million in 2003) was \$150 million in 2005, \$149 million in 2004 and \$137 million in 2003.

Note 19 Pension And Other Postretirement Benefit Plans

The Company and certain of its subsidiaries have defined benefit pension plans, defined contribution plans, and termination indemnity plans for regular full-time employees. The principal pension plan is the Bristol-Myers Squibb Retirement Income Plan. The funding policy is to contribute amounts to provide for current service and to fund past service liability. Plan benefits are based primarily on the participant's years of credited service and compensation. Plan assets consist principally of equity and fixed-income securities.

The Company also provides comprehensive medical and group life benefits for substantially all U.S. retirees who elect to participate in its comprehensive medical and group life plans. The medical plan is contributory. Contributions are adjusted periodically and vary by date of retirement and the original retiring Company. The life insurance plan is noncontributory. Plan assets consist principally of equity and fixed-income securities. Similar plans exist for employees in certain countries outside of the United States.

Cost of the Company's deferred benefits and postretirement benefit plans included the following components:

Dollars in Millions	Pension Benefits			Other Benefits		
	2005	2004	2003	2005	2004	2003
Service cost — benefits earned during the year	\$ 223	\$ 180	\$ 144	\$ 9	\$ 8	\$ 8
Interest cost on projected benefit obligation	314	295	275	36	37	46
Expected return on plan assets	(361)	(355)	(353)	(20)	(18)	(15)
Net amortization and deferral	216	157	71	3	—	7
Net periodic benefit cost	392	277	137	28	27	46
Curtailments and settlements	—	(1)	(1)	—	—	—
Total net periodic benefit cost	\$ 392	\$ 276	\$ 136	\$ 28	\$ 27	\$ 46

The Company has recognized the impact of the Medicare Prescription Drug Improvement and Modernization Act of 2003 in 2005 and 2004, and in accordance with FSP No. 106-2, recorded \$11 million and \$8 million in 2005 and 2004, respectively, as a reduction in net periodic benefit costs.

Changes in benefit obligations and plan assets for December 31, 2005 and 2004, for the Company's defined benefit and postretirement benefit plans, were:

	Pension Benefits		Other Benefits	
Dollars in Millions	2005	2004	2005	2004
Benefit obligation at beginning of year	\$ 5,481	\$ 4,755	\$ 646	\$ 758
Service cost—benefits earned during the year	223	180	9	8
Interest cost on projected benefit obligation	314	295	36	37
Plan participants' contributions	3	3	8	6
Curtailments and settlements	(2)	(3)	—	—
Actuarial losses/(gains)	400	533	17	(78)
Plan amendments	—	(4)	—	(17)
Benefits paid	(386)	(399)	(73)	(68)
Exchange rate (gains)/losses	(115)	121	—	—
Benefit obligation at end of year	\$ 5,918	\$ 5,481	\$ 643	\$ 646
Fair value of plan assets at beginning of year	\$ 4,602	\$ 4,085	\$ 230	\$ 205
Actual return on plan assets	469	456	23	25
Employer contribution	423	367	65	62
Plan participants' contributions	3	3	8	6
Settlements	(1)	—	—	—
Transfer in/(out)	—	(3)	—	—
Benefits paid	(386)	(399)	(73)	(68)
Exchange rate (losses)/gains	(93)	93	—	—
Fair value of plan assets at end of year	\$ 5,017	\$ 4,602	\$ 253	\$ 230
Funded status	\$ (901)	\$ (879)	\$ (390)	\$ (416)
Unamortized net obligation at adoption	2	3	—	—
Unrecognized prior service cost	61	74	(27)	(31)
Unrecognized net actuarial loss	2,067	2,017	108	103
Net amount recognized	\$ 1,229	\$ 1,215	\$ (309)	\$ (344)
Amounts recognized in the balance sheet consist of:				
Prepaid benefit cost	\$ 1,324	\$ 1,272	\$ —	\$ —
Accrued benefit cost	(423)	(406)	(309)	(344)
Intangible assets	2	3	—	—
Accumulated other comprehensive loss	326	346	—	—
Net amount recognized	\$ 1,229	\$ 1,215	\$ (309)	\$ (344)

Several plans had underfunded accrued benefit obligations that exceeded their accrued benefit liabilities at December 31, 2005 and 2004. Additional minimum liabilities were established to increase the accrued benefit liabilities to the values of the underfunded accrued benefit obligations. The additional minimum liabilities totaled \$328 million and \$349 million at December 31, 2005 and 2004, respectively, for a U.S. unfunded benefit equalization plan and several international plans. The additional minimum liabilities were offset by intangible assets of \$2 million and \$3 million and charges to other comprehensive income included in stockholders' equity of \$326 million and \$346 million at December 31, 2005 and 2004, respectively.

The accumulated benefit obligation for all defined benefit pension plans was \$5,209 million and \$4,828 million at December 31, 2005 and 2004, respectively.

Information for pension plans with accumulated benefit obligations in excess of plan assets was:

	December 31,	
Dollars in Millions	2005	2004
Projected benefit obligation	\$ 1,343	\$ 1,313
Accumulated benefit obligation	1,148	1,139
Fair value of plan assets	748	742

This is attributable primarily to an unfunded U.S. benefit equalization plan and several plans in the international markets. The unfunded U.S. benefit equalization plan provides pension benefits for employees with compensation above IRS limits and cannot be funded in a tax-advantaged manner.

Additional information pertaining to the Company's pension and postretirement plans:

Dollars in Millions	Pension Benefits			Other Benefits		
	2005	2004	2003	2005	2004	2003
(Decrease)/Increase in minimum liability, including the impact of foreign currency fluctuations, included in other comprehensive income	\$ (20)	\$ 153	\$ 53	\$ —	\$ —	\$ —

Weighted-average assumptions used to determine benefit obligations at December 31, were:

	Pension Benefits		Other Benefits	
	2005	2004	2005	2004
Discount rate	5.49%	5.57%	5.49%	5.52%
Rate of compensation increase	3.60%	3.59%	3.61%	3.59%

Weighted-average actuarial assumptions used to determine net periodic benefit cost for the years ended December 31, were:

	Pension Benefits			Other Benefits		
	2005	2004	2003	2005	2004	2003
Discount rate	5.57%	6.08%	6.56%	5.52%	6.01%	6.75%
Expected long-term return on plan assets	8.41%	8.73%	8.81%	8.75%	9.00%	9.00%
Rate of compensation increase	3.59%	3.57%	3.33%	3.59%	3.58%	3.29%

At December 31, 2005, the Company's expected long-term rate of return on U.S. pension plan assets was 8.75%. The target asset allocation is 70% public equity (58% U.S., 12% international), 8% private equity and 22% fixed income. The 8.75% was approximated by applying expected returns of 9% on public equity, 15% on private equity and 6% on fixed income to the target allocation. The actual historical returns are also relevant. Annualized returns for periods ended December 31, 2005 were 9.6% for 10 years, 10.9% for 15 years and 10.5% for 20 years.

U.S. pension plan assets represented approximately 80% of total Company pension plan assets at December 31, 2004. The 8.41% disclosed above for total Company expected return on assets for 2005 is below the 8.75% for U.S. pension plans due to the impact of international pension plans, which typically employ a less aggressive asset allocation.

An 8.75% expected return is disclosed for Other Benefits in 2005 as the relevant assets are invested in the same manner as U.S. pension plan assets and there are no international plan assets.

Assumed health care cost trend rates at December 31, were:

	2005	2004	2003
Health care cost trend rate assumed for next year	7.93%	8.93%	9.96%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	4.42%	4.51%	4.50%
Year that the rate reaches the ultimate trend rate	2012	2012	2010

Assumed health care cost trend rates do have an effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

Dollars in Millions	1-Percentage-Point Increase	1-Percentage-Point Decrease
Effect on total of service and interest cost	\$ 1	\$ (1)
Effect on postretirement benefit obligation	22	(17)

The Company's asset allocation for pension and postretirement benefits at December 31, 2005 and 2004, was:

	Pension Benefits		Other Benefits	
	2005	2004	2005	2004
Public equity securities	67.3%	68.9%	67.7%	69.9%
Debt securities (including cash)	26.8	25.5	25.0	23.4
Private equity	5.6	5.2	7.1	6.5
Other	0.3	0.4	0.2	0.2
Total	100.0%	100.0%	100.0%	100.0%

The Company's investment strategy emphasizes equities in order to achieve high expected returns and, in the long run, low expense and low required cash contributions. For the U.S. pension plans, a target asset allocation of 70% public equity (58% U.S., 12% international), 8% private equity and 22% fixed income is maintained and cash flow (i.e., cash contributions, benefit payments) is used to rebalance back to the targets as necessary. Investments are very well diversified within each of the three major asset categories. About 40% of the U.S. equity is passively managed. Otherwise, all investments are actively managed.

Investment strategies for international pension plans are typically similar, although the asset allocations are usually more conservative.

Bristol-Myers Squibb Company common stock represents less than 1% of the plan assets at December 31, 2005 and 2004.

Assets for postretirement benefits are commingled with U.S. pension plan assets and, therefore, the investment strategy is identical to that described above for U.S. pension plans.

Contributions

Although no minimum contributions will be required, the Company plans to make cash contributions to the U.S. pension plans in 2006.

When contributions are made to the U.S. pension plans, the Company may make tax-deductible contributions to the 401(h) account for retiree medical benefits equal to a portion of the pension normal cost.

Contributions to the international pension plans are now expected to be in the \$70 to \$90 million range for 2006.

Estimated Future Benefit Payments

The following benefit payments for mainly the U.S. pension plans, which reflect expected future service, as appropriate, are expected to be paid:

Dollars in Millions	Pension Benefits	Other Benefits		
		Gross	Medicare Subsidy	Net
2006	\$ 280	\$ 67	\$ 7	\$ 60
2007	300	65	8	57
2008	324	64	8	56
2009	338	64	9	55
2010	357	62	9	53
Years 2011 – 2015	2,159	293	51	242

Savings Plan

The principal defined contribution plan is the Bristol-Myers Squibb Savings and Investment Program. The Company's contribution is based on employee contributions and the level of Company match. The Company's contributions to the plan were \$51 million in 2005, \$53 million in 2004 and \$51 million in 2003.

Termination Indemnity Plans

The Company operates in certain jurisdictions, primarily in Europe, which require the recording of statutory termination obligations. These obligations were assessed in accordance with EITF 88-1, *Determination of Vested Benefit Obligation for a Defined Benefit Pension Plan*. The total liability recorded for these obligations was \$68 million at December 31, 2005 and \$81 million at December 31, 2004.

Note 20 Legal Proceedings and Contingencies

Various lawsuits, claims, proceedings and investigations are pending against the Company and certain of its subsidiaries. In accordance with SFAS No. 5, *Accounting for Contingencies*, the Company records accruals for such contingencies when it is probable that a liability will be incurred and the amount of loss can be reasonably estimated. These matters involve antitrust, securities, patent infringement, pricing, sales and marketing practices, environmental, health and safety matters, product liability and insurance coverage. The most significant of these matters are described below. There can be no assurance that there will not be an increase in the scope of these matters or that any future lawsuits, claims, proceedings or investigations will not be material. Management continues to believe, as previously disclosed, that during the next few years, the aggregate impact, beyond current reserves, of these and other legal matters affecting the Company is reasonably likely to be material to the Company's results of operations and cash flows, and may be material to its financial condition and liquidity.

The Company's decision to obtain insurance coverage is dependent on market conditions, including cost and availability, existing at the time such decisions are made. As a result of external factors, the availability of insurance has become more restrictive while the cost has increased significantly. The Company has evaluated its risks and has determined that the cost of obtaining insurance outweighs the benefits of coverage protection against losses and as such, became self-insured for product liabilities effective July 1, 2004. The Company will continue to evaluate these risks and benefits to determine its insurance needs in the future.

INTELLECTUAL PROPERTY

Plavix Litigation

Plavix is currently the Company's largest product ranked by net sales. Net sales of Plavix were approximately \$3.8 billion for the year ended December 31, 2005. The Plavix patents are subject to a number of challenges in the United States and Canada as described below.

Currently, the Company expects Plavix to have market exclusivity in the United States until 2011. Apotex announced that on January 2006 it had received final approval of its aNDA for clopidogrel bisulfate from the FDA. Accordingly, Apotex could decide to launch a generic product at risk at any time. Such generic competition would likely result in substantial decreases in the sales of Plavix in the United States. The Company expects that the final approval of the aNDAs of the other defendants will be subject to any potential 180-day semi-exclusivity of Apotex.

United States

The Company's U.S. territory partnership under its alliance with Sanofi is a plaintiff in four pending patent infringement lawsuits instituted in the U.S. District Court for the Southern District of New York entitled Sanofi-Synthelabo, Sanofi-Synthelabo Inc., and Bristol-Myers Squibb Sanofi Pharmaceuticals Holding Partnership v. Apotex Inc. and Apotex Corp. (Apotex), 02-CV-2255 (SHS); Sanofi-Synthelabo, Sanofi-Synthelabo Inc. and Bristol-Myers Squibb Sanofi Pharmaceuticals Holding Partnership v. Dr. Reddy's Laboratories, LTD, and Dr. Reddy's Laboratories, Inc., 02-CV-3672 (SHS); Sanofi-Synthelabo, Sanofi-Synthelabo Inc., and Bristol-Myers Squibb Sanofi Pharmaceuticals Holding Partnership v. Teva Pharmaceuticals USA, Inc. and Teva Pharmaceuticals Industries, Ltd., 04-CV-7458 and Sanofi-Aventis, Sanofi-Synthelabo Inc., and Bristol-Myers Squibb Sanofi Pharmaceuticals Holding Partnership v. Cobalt Pharmaceuticals Inc., 05-CV-8055 (SHS). Teva Pharmaceuticals Industries, Ltd. has since been dismissed from the case. Proceedings involving Plavix are also in progress in Canada.

The U.S. suits were filed on March 21, 2002, May 14, 2002, September 23, 2004 and September 16, 2005 respectively, and were based on U.S. Patent No. 4,847,265, a composition of matter patent, which discloses and claims, among other things, the hydrogen sulfate salt of clopidogrel, which is marketed as Plavix. The first two suits were also based on U.S. Patent No. 5,576,328, which discloses and claims, among other things, the use of clopidogrel to prevent a secondary ischemic event. The plaintiffs later withdrew Patent No. 5,576,328 from the two lawsuits. Plaintiffs' infringement position is based on defendants' filing of their Abbreviated New Drug Applications (aNDA) with the FDA, seeking approval to sell generic clopidogrel bisulfate prior to the expiration of the composition of matter patent in 2011. The defendants responded by alleging that the patent is invalid and/or unenforceable. Apotex has added antitrust counterclaims. The first two cases were consolidated for discovery. Fact discovery closed on October 15, 2003 and expert discovery was completed in November 2004. The joint pretrial order in the Apotex case was submitted May 27, 2005, and the court approved it.

The court has scheduled trial in the Apotex matter to begin in June 2006. The Apotex case will be tried without a jury. Plaintiffs filed a motion to consolidate the Dr. Reddy's case with the Apotex case for trial. That motion is pending before the court. In a stipulation approved by the U.S. District Court for the Southern District of New York on April 15, 2005, all parties to the patent infringement litigation against Teva have agreed that the Teva litigation will be stayed, pending resolution of the Apotex and Dr. Reddy's litigation, and that the parties to the Teva litigation will be bound by the outcome of the litigation in the District Court against Apotex or Dr. Reddy's. On April 18, 2005, the Court denied as moot the pending motion to consolidate the Teva litigation with the litigation against Apotex and Dr. Reddy's, as a result of the Court's approval of the stipulation. The parties submitted a similar stipulation to the court in the Cobalt case on October 12, 2005, and the Court approved it. Thus the case against Cobalt is also stayed.

On April 20, 2005, Apotex filed a complaint for declaratory judgment against Sanofi-Aventis, Sanofi-Aventis, Inc., and Bristol-Myers Squibb Sanofi Pharmaceuticals Holding Partnership. The complaint seeks a declaratory judgment that the '265 patent is unenforceable due to alleged inequitable conduct committed during the prosecution of the patent. The defendants responded by submitting a motion to dismiss, which the court granted on September 12, 2005. Apotex has filed an appeal to the United States Court of Appeals for the Federal Circuit.

The Company's U.S. territory partnership under its alliance with Sanofi is a plaintiff in another pending patent infringement lawsuit instituted in the U.S. District Court for the District of New Jersey entitled Sanofi-Synthelabo, Sanofi-Synthelabo Inc. and Bristol-Myers Squibb Sanofi Pharmaceuticals Holding Partnership v. Watson Pharmaceuticals, Inc. and Watson Laboratories, Inc. 2:04-CV-4926. The suit was filed October 7, 2004 and was based on U.S. patent 6,429,210, which discloses and claims a particular crystalline or polymorph form of the hydrogen sulfate salt of clopidogrel, which is marketed as Plavix. The case is in the discovery phase. On December 8, 2005, the court permitted Watson to pursue its declaratory judgment counterclaim with respect to U.S. Patent No. 6,504,030. On January 24, 2006, the Court approved the parties' stipulation to stay this case pending the outcome of the trial in the Apotex matter. Thus this case is officially stayed.

Canada

Sanofi-Synthelabo and Sanofi-Synthelabo Canada Inc. instituted a prohibition action in the Federal Court of Canada against Apotex Inc. (Apotex) and the Minister of Health in response to a Notice of Allegation (NOA) from Apotex directed against Canadian Patent 1,336,777 covering clopidogrel bisulfate. Apotex's Notice of Allegation indicated that it had filed an Abbreviated New Drug Submission (ANDS) for clopidogrel bisulfate tablets and that it sought approval (a Notice of Compliance) of that ANDS before the expiration of Canadian Patent 1,336,777, which expires August 12, 2012. Apotex's NOA further alleged that the '777 patent was invalid or not infringed. A hearing was held from February 21 to February 25, 2005. On March 21, 2005, the Canadian Federal Court of Ottawa rejected Apotex's challenge to the Canadian Plavix patent and held that the asserted claims are novel, not obvious and infringed, and granted Sanofi's application for an order of prohibition against the Minister of Health and Apotex Inc. That order of prohibition will preclude approval of Apotex's ANDS until the patent expires in 2012, unless the Federal Court's decision is reversed on appeal. Apotex has filed an appeal.

Sanofi-Synthelabo and Sanofi-Synthelabo Canada Inc. also instituted a prohibition action in the Federal Court of Canada against Apotex and the Minister of Health in response to a NOA directed against Canadian Patent 2,334,870 covering the form 2 polymorph of clopidogrel bisulfate. Apotex seeks approval of its ANDS before expiration of the '870 patent in 2019. Apotex alleges in its NOA that it does not infringe the '870 patent and that it is invalid. That action was discontinued.

Sanofi-Aventis and Sanofi-Synthelabo Canada Inc. instituted a prohibition action in the Federal Court of Canada against Novopharm Limited (Novopharm) and the Minister of Health in response to a Notice of Allegation from Novopharm directed against Canadian Patent 1,336,777 covering clopidogrel bisulfate. Novopharm's NOA indicated that it had filed an ANDS for clopidogrel bisulfate tablets and that it sought approval (a Notice of Compliance) of that ANDS before the expiration of Canadian Patent 1,336,777, which expires August 12, 2012. Novopharm's NOA further alleged that the '777 patent was invalid. Novopharm has since withdrawn its NOA and agreed to be bound by the result in the Apotex proceeding. The prohibition action has therefore been discontinued.

Sanofi-Aventis and Sanofi-Synthelabo Canada Inc. instituted a prohibition action in the Federal Court of Canada against Cobalt Pharmaceuticals Inc. and the Minister of Health in response to a Notice of Allegation from Cobalt directed against Canadian patents 1,336,777 and 2,334,870. Cobalt's NOA indicated that it has filed an ANDS for clopidogrel bisulfate tablets and that it sought a Notice of Compliance for that ANDS before the expiration of the '777 and '870 patents. Cobalt alleged that the '777 patent was invalid and that the '870 patent was invalid and not infringed. The case has been stayed pending the outcome of the Apotex appeal.

Although the plaintiffs intend to vigorously pursue enforcement of their patent rights in Plavix, it is not possible at this time reasonably to assess the outcome of these lawsuits, or, if the Company were not to prevail in these lawsuits, or, if Apotex, which now has final approval of its aNDA in the U.S. were to enter the market with a generic product at risk, the timing of potential generic competition for Plavix. It also is not possible reasonably to estimate the impact of these lawsuits on the Company.

However, loss of market exclusivity of Plavix and the subsequent development of generic competition would be material to the Company's sales of Plavix and results of operations and cash flows, and could be material to its financial condition and liquidity. See Note 8 "Income Taxes" for additional information.

OTHER INTELLECTUAL PROPERTY LITIGATION

Tequin. The Company and Kyorin Pharmaceuticals Co., Ltd. (Kyorin) commenced a patent infringement action on March 23, 2004, against Teva USA and Teva Industries in the United States District Court for the Southern District of New York, relating to the antibiotic gatifloxacin, for which Kyorin holds the composition of matter patent and which the Company sells as *Tequin*. Teva Industries has since been dismissed from the case. This action relates to Teva's filing of an aNDA for a generic version of gatifloxacin tablets with a certification that the composition of matter patent, which expires in December 2007 but which has been granted a patent term extension until December 2009, is invalid or not infringed. The filing of the suit places a stay on the approval of Teva's generic product until June 2007, unless there is a court decision adverse to the Company and Kyorin before that date. Trial in this matter has been scheduled to begin on May 1, 2006.

Tequin (injectable form). The Company and Kyorin commenced patent infringement actions on March 8, 2005, against Apotex Inc. and Apotex Corp., and against Sicor Pharmaceuticals, Inc., Sicor Inc., Sicor Pharmaceuticals Sales Inc., Teva Pharmaceuticals USA, Inc., and Teva Pharmaceutical Industries Ltd. in the United States District Court for the Southern District of New York, relating to injectable forms of the antibiotic gatifloxacin, for which Kyorin holds the composition of matter patent and which the Company sells as *Tequin*. The action related to Apotex's and Sicor's filing of aNDAs for generic versions of injectable gatifloxacin with p(IV) certifications that the composition of the matter patent, which expires December 2007 but which was granted a patent term extension until December 2009, is invalid. The filing of the lawsuits places stays on the approvals of both Apotex's and Sicor's generic products until July/August 2007, unless there is a court decision adverse to the Company and Kyorin before that date. The Sicor case was consolidated with the above proceeding. In a stipulation approved by the U.S. District Court for the Southern District of New York on August 22, 2005, the parties agreed that the Apotex case will be stayed pending resolution of the Teva and Sicor cases, and that the parties will be bound by the outcome of the above litigation.

Erbix. On October 28, 2003, a complaint was filed by Yeda Research and Development Company Ltd. (Yeda) against ImClone and Aventis Pharmaceuticals, Inc. in the U.S. District Court for the Southern District of New York. This action alleges and seeks that three individuals associated with Yeda should also be named as co-inventors on U.S. Patent No. 6,217,866, which covers the therapeutic combination of any EGFR-specific monoclonal antibody and anti-neoplastic agents, such as chemotherapeutic agents, for use in the treatment of cancer. If Yeda's action were successful, Yeda could be in a position to practice, or to license others to practice, the invention. This could result in product competition for Erbix that might not otherwise occur. The Company, which is not a party to this action, is unable to predict the outcome at this stage in the proceedings.

On May 5, 2004, Repligen Corporation (Repligen) and Massachusetts Institute of Technology (MIT) filed a lawsuit in the United States District Court for the District of Massachusetts against ImClone, claiming that ImClone's manufacture and sale of Erbitux infringes a patent that generally covers a process for protein production in mammalian cells. Repligen and MIT seek damages based on sales of Erbitux which commenced in February 2004. The patent expired on May 5, 2004, although Repligen and MIT are seeking extension of the patent. The Company, which is not a party to this action, is unable to predict the outcome at this stage in the proceedings.

Orencia. On January 6, 2006, Repligen Corporation (Repligen) and the Regents of the University of Michigan filed a complaint against the Company in the United States District Court for the Eastern District of Texas, Marshall Division. The complaint alleges that the Company's anticipated sale of Orencia will infringe U.S. Patent 6,685,541.

Abilify. On August 11, 2004, Otsuka filed with the United States Patent and Trademark Office (USPTO) a Request for Reexamination of U.S. composition of matter patent covering Abilify, an antipsychotic agent used for the treatment of schizophrenia and related psychiatric disorders (U.S. Patent Number No. 5,006,528, the "528 Patent") that expires in 2014, including granted supplemental protection extensions. Otsuka has determined that the original '528 Patent application contained an error in that the description of a prior art reference was identified by the wrong patent number. In addition, Otsuka has taken the opportunity to bring other information to the attention of the USPTO. The USPTO has granted the Request for Reexamination and the reexamination proceeding is ongoing. The reexamination proceeding will allow the USPTO to consider the patentability of the patent claims in light of the corrected patent number and newly cited information. The USPTO is expected to make a final decision on the reexamination before the end of 2006. The Company's rights to commercialize the product in the U.S. expire in November 2012.

The Company and Otsuka believe that the invention claimed in the '528 Patent is patentable over the prior art and expect that the USPTO will reconfirm that in the reexamination. However, there can be no guarantee as to the outcome. If the patentability of the '528 Patent were not reconfirmed following a reexamination, there may be sooner than expected loss of market exclusivity of Abilify and the subsequent development of generic competition, which would be material to the operating results of the Company.

SECURITIES LITIGATION

Vanlev Litigation

In April, May and June 2000, the Company, its former chairman of the board and chief executive officer, Charles A. Heimbold, Jr., and its former chief scientific officer, Peter S. Ringrose, Ph.D., were named as defendants in a number of class action lawsuits alleging violations of federal securities laws and regulations. These actions were consolidated into one action in the U.S. District Court for the District of New Jersey. The plaintiff claimed that the defendants disseminated materially false and misleading statements and/or failed to disclose material information concerning the safety, efficacy and commercial viability of *Vanlev*, a drug in development, during the period November 8, 1999 through April 19, 2000.

A number of related class actions, making essentially the same allegations, were also filed in the U.S. District Court for the Southern District of New York. These actions were transferred to the U.S. District Court for the District of New Jersey. The court certified two separate classes: a class relating to the period from November 8, 1999 to April 19, 2000 (the "First Class Period") and a class relating to the period from March 22, 2001 to March 20, 2002 (the "Second Class Period"). The First Class Period involved claims related to *Vanlev*'s efficacy, safety and/or potential to be a blockbuster drug. The Second Class Period involved claims related to *Vanlev*'s potential to be a blockbuster drug. The class certifications were without prejudice to defendants' rights to fully contest the merits of plaintiff's claims. The plaintiff sought compensatory damages, costs and expenses on behalf of shareholders with respect to the two class periods. On December 17, 2004, the Company and the other defendants made a motion for summary judgment as to all of plaintiff's claims. On August 17, 2005, the Court granted in part and denied in part the summary judgment motion and also dismissed two of the three individual defendants, Peter R. Dolan and Peter S. Ringrose, from the case.

On February 8, 2006, the court granted preliminary approval of a settlement agreement between the parties under which the Company will pay \$185 million into a settlement fund and agree to certain non-monetary terms. The settlement is subject to certain conditions including final approval at a fairness hearing scheduled for May 11, 2006. Accordingly, the Company established a reserve in the fourth quarter of 2005 and the \$185 million was paid to the settlement fund in February 2006.

Other Securities Matters

In 2002 and 2003, the Company and certain of its current and former officers and PricewaterhouseCoopers were named as defendants in a number of securities class actions and derivative suits in the United States District Court for the Southern District of New York. These lawsuits alleged violations of federal securities laws and regulations in connection with sales incentives and wholesaler inventory levels, breaches of fiduciary duty in connection with the Company's conduct concerning, among other things: safety, efficacy and commercial viability of *Vanlev* (as discussed above); the Company's sales incentives to certain wholesalers and the inventory levels of those wholesalers; the Company's investment in and relations with ImClone and ImClone's product Erbitux; and alleged anticompetitive behavior in connection with *BuSpar* and *TAXOL*® (paclitaxel). The suits have all been settled with respect to the Company and its current and former officers and directors.

On September 21, 2005, certain of the Company's current and former officers were named in a purported class action, *Starkman v. Bristol-Myers Squibb et al.*, filed in New York State Supreme Court alleging factual claims similar to the now resolved federal class action in the Southern District of New York noted above, and asserted common law fraud and breach of fiduciary duty claims on behalf of stockholders who purchased the Company's stock before October 19, 1999 and held their stock through March 10, 2003. On October 7, 2005, the Company removed the case to the United States District Court for the Southern District of New York. The case is currently stayed.

On November 18, 2004, a class action complaint was filed in the United States District Court for the Eastern District of Missouri against the Company, D&K Health Care Resources, Inc. ("D&K") and several current and former D&K directors and officers on behalf of purchasers of D&K stock between August 10, 2000 and September 16, 2002. The complaint alleges that the Company participated in fraudulently inflating the value of D&K stock by allegedly engaging in improper "channel-stuffing" agreements with D&K. The Company filed a motion to dismiss this case on January 28, 2005. That motion is under consideration by the court. Under the Private Securities Litigation Reform Act, discovery is automatically stayed pending the outcome of the motion to dismiss. The plaintiff has moved to partially lift the automatic stay. The court is considering that motion.

These last two cases noted above are at very preliminary stages, and the Company is unable to assess the outcome or to reasonably estimate possible loss or range of loss with respect to these cases.

On August 4, 2004, the Company entered into a final settlement with the SEC, concluding an investigation concerning certain wholesaler inventory and accounting matters. The Company agreed, without admitting or denying any liability, not to violate certain provisions of the securities laws. The Company also established a \$150 million fund, which will be distributed to certain Company shareholders under a plan of distribution established by the SEC.

The settlement does not resolve the ongoing investigation by the SEC of the activities of certain current and former members of the Company's management in connection with the wholesaler inventory issues and other accounting matters. The Company is continuing to cooperate with this investigation.

On June 15, 2005, the United States Attorney's Office for the District of New Jersey ("the Office") filed a criminal complaint charging the Company with conspiracy to commit securities fraud in connection with a previously disclosed investigation by that Office, concerning the inventory and various accounting matters covered by the Company's settlement with the SEC. In connection with the filing of that complaint, the Company and the Office entered into a Deferred Prosecution Agreement. Pursuant to that Agreement, the Company agreed to maintain and continue to implement remedial measures pursuant to the settlement with the SEC, take certain additional remedial actions, appoint an Independent Monitor and continue to cooperate with the Office, including with respect to the ongoing investigation regarding individual current and former employees of the Company, as well as to make an additional payment of \$300 million into the fund for shareholders established pursuant to the Company's settlement with the SEC. If the Company fulfills its obligations under the Deferred Prosecution Agreement, the Office will dismiss the criminal complaint two years from the date of its filing.

Pricing, Sales and Promotional Practices Litigation and Investigations

The Company, together with a number of other pharmaceutical manufacturers, is a defendant in private class actions, as well as suits brought by the Attorneys General of several states and by numerous New York Counties and the City of New York that are pending in federal and state courts relating to the pricing of Company products. The federal cases have been consolidated for pre-trial purposes under the caption *In re Pharmaceutical Industry Average Wholesale Price Litigation*, MDL No. 1456 in the U.S. District Court for the District of Massachusetts (the "AWP MDL").

The pleadings in the private class action have been amended over the course of the AWP MDL in response to the Court's rulings on both class certification and merits issues. On October 16, 2005, the plaintiffs filed their Third Amended Master Consolidated Class Action Complaint ("TAMCC") alleging that the Company's and many other pharmaceutical manufacturers' reporting of prices for certain prescription drug products (20 listed drugs in the Company's case) had the effect of falsely overstating the Average Wholesale Price ("AWP") published in industry compendia, which in turn improperly inflated the reimbursement paid to medical providers and others who prescribed and administered those products. The TAMCC asserts claims under the federal RICO statute, state consumer protection and fair trade statutes; however, because of the Court's prior rulings, the RICO claims have been dismissed and they continue to be included in the TAMCC primarily for appeal purposes. In addition, in an opinion dated August 16, 2005, the Court declined to certify any proposed class as to those of the Company's drugs that are self-administered by the patient (i.e., pills, liquids that can be purchased in a pharmacy) and expressed a willingness to certify only classes involving those drugs that are administered by a physician (e.g. injectables such as oncology drugs). On January 19, 2006, the Court heard argument on the certification of three classes of persons and entities who paid for or reimbursed for seven of the Company's physician-administered drugs and certified the following classes: (i) a nationwide class of individual Medicare Part B beneficiaries; (ii) a Massachusetts class of "Medigap" insurers; and (iii) a Massachusetts class of entities and persons in private commerce who paid or were reimbursed for the drugs based on AWP. Fact discovery by the plaintiffs of the Company is closed in the private AWP MDL proceedings and the case is progressing on issues of expert discovery. On January 31, 2006, the Court issued a case management order scheduling summary judgment motions to be filed on March 15, 2006 and setting a trial date for the Company of November 6, 2006.

Certain of the State Attorneys General actions and suits of New York Counties and New York City are also proceeding in the AWP MDL. Specifically, the Company is a defendant in complaints by the Montana, Illinois, Kentucky and California Attorneys General, as well as a master consolidated complaint of 42 New York Counties and of New York City and a complaint by Nassau County, New York. Other Attorneys General suits are proceeding against the Company, among many other drug manufacturers, in the state courts of Pennsylvania, Nevada, Wisconsin, Alabama and Mississippi. The Company and other defendants removed to federal court a recent state court case filed by the Arizona Attorney General. Defendants will seek to transfer that case to the AWP MDL. Finally, the Company is one of many defendants in a case commenced by Erie County, New York, that is proceeding in state court. The allegations in the various State Attorneys General and New York County and New York City cases are similar to those in the private class action in the AWP MDL in the following respect: they all allege that the Company and the other manufacturers caused AWP's to be inflated, thereby injuring entities and persons who reimbursed prescription drugs based on AWP's. The primary differences from the AWP MDL are: (a) the States and Counties sue on behalf of themselves as payors for drugs under State Medicaid programs, as well as on behalf of corporate and individual citizens in their States who paid or reimbursed for drugs based on AWP's; (b) the States and Counties either do not limit or cite a greater number of drugs for which they contend AWP's were inflated; and (c) certain States and New York Counties also allege that the Company and the other defendants underpaid the amount of "rebates" owed them under the Medicaid rebate statute and a rebate agreement with the federal government. Finally, the Company is also a defendant in one private class action pending in Arizona state court that contains allegations similar to those made in the AWP MDL. No class has been certified in that case, which has been stayed pending the resolution of the class motions in the AWP MDL.

The Company is also a defendant in two putative class actions involving its prices under Section 340B of the Public Health Services Act, which requires prescription drug manufacturers to offer discounts to qualified medical providers – generally those who disproportionately service poor people. In one case, pending in Alabama federal court, the plaintiffs are two medical providers who claim that they and all other providers across the country did not receive the discounted prices to which they were entitled. In the other case, pending in California federal court, the County of Santa Clara, California, contends that it and other counties and cities in California have had to provide more financing to local hospitals than otherwise would have been necessary had the Company and the other defendants provided the appropriate discounts. The Alabama court denied defendants' motion to dismiss. On February 14, 2006, the motion to dismiss in the California action was granted. The Court also granted plaintiff leave to amend, and the plaintiff has filed an amended complaint. These cases are at a preliminary stage, and the Company is unable to assess the outcome and any possible effects on its business and profitability, or reasonably estimate possible loss or range of loss with respect to these cases. If the Company were not to prevail in final, non-appealable determinations of these litigations, the impact could be material.

The Company, together with a number of other pharmaceutical manufacturers, also has received subpoenas and other document requests from various government agencies seeking records relating to its pricing, sales and marketing practices, and "Best Price" reporting for drugs covered by Medicare and/or Medicaid and by the Public Health Service Act 340B program. The requests for records have come from the U.S. Attorneys' Offices for the District of Massachusetts, the Eastern District of Pennsylvania, and the Northern District of Texas, the Civil Division of the Department of Justice, the Offices of the Inspector General of the Department of Health and Human Services and the Office of Personnel Management (each in conjunction with the Civil Division of the Department of Justice), the Office of Pharmacy Assistance of the Health Resources and Services Administration (HRSA), and several states. In addition, requests for information have come from the House Committee on Energy & Commerce and the Senate Finance Committee in connection with investigations that the committees are currently conducting into Medicaid Best Price issues and the use of educational grants by pharmaceutical companies.

As previously disclosed, in mid-2003, the Company initiated an internal review of certain of its sales and marketing practices, focusing on whether these practices comply with applicable anti-kickback laws and analyzing these practices with respect to compliance with (1) Best Price reporting and rebate requirements under the Medicaid program and certain other U.S. governmental programs, which reference the Medicaid rebate program and (2) applicable FDA requirements. The Company has met with representatives of the U.S. Attorney's Office for the District of Massachusetts to discuss the review and has received related subpoenas from that U.S. Attorney's Office, including a subpoena received on May 5, 2005, for documents relating to possible off label promotion of Abilify. The Company's internal review is expected to continue until resolution of pending governmental investigations of related matters.

The Company is producing documents and actively cooperating in the investigations, which could result in the assertion of civil and/or criminal claims. The Company has reserves for liabilities in relation to pharmaceutical pricing and sales and marketing practices of \$146 million. It is not possible at this time to reasonably assess the final outcome of these matters. In accordance with GAAP, the Company has determined that the above amount represents minimum expected probable losses with respect to these matters, which losses could include the imposition of fines, penalties, administrative remedies and/or liability for additional rebate amounts. Eventual losses related to these matters may exceed these reserves, and the further impact could be material. The Company does not believe that the top-end of the range for these losses can be estimated. If the Company were not to prevail in final, non-appealable determinations of these investigations, the impact could be material.

As previously disclosed, in 2004 the Company undertook an analysis of its methods and processes for calculating prices for reporting under governmental rebate and pricing programs related to its U.S. Pharmaceuticals business. The analysis was completed in early 2005. Based on the analysis, the Company identified the need for revisions to the methodology and processes used for calculating reported pricing and related rebate amounts and implemented these revised methodologies and processes beginning with its reporting to the Federal government agency with primary responsibility for these rebate and price reporting obligations, the Centers for Medicare and Medicaid Services (CMS) in the first quarter of 2005. In addition, using the revised methodologies and processes, the Company also has recalculated the "Best Price" and "Average Manufacturer's Price" required to be reported under the Company's federal Medicaid rebate agreement and certain state agreements, and the corresponding revised rebate liability amounts under those programs for the three-year period 2002 to 2004. Upon completion of the analysis in early 2005, the Company determined that the estimated rebate liability for those programs for the three-year period 2002 to 2004 was actually less than the rebates that had been paid by the Company for such period. Accordingly, in the fourth quarter of 2004, the Company recorded a reduction to the rebate liability in the amount of the estimated overpayment. The Company has submitted proposed revisions and an updated estimate to CMS for review, and more recently has notified the government that it will be submitting a further updated estimate correcting recently identified programming errors. The Department of Justice (DOJ) has informed the Company that it also is reviewing the submission in conjunction with the previously disclosed subpoena received by the Company from the DOJ relating to, among other things, "Best Price" reporting for drugs covered by Medicaid as discussed in more detail above, and has requested the Company to provide additional information regarding the proposed revisions and estimate. These agencies may take the position that further revisions to the Company's methodologies and calculations are required. The Company believes, however, based on current information, that any such recalculation for 2002-2004 period is not likely to result in material rebate liability. However, due to the uncertainty surrounding the recoverability of the Company's estimated overpayment arising from the review process described above, the Company recorded a reserve in an amount equal to the estimated overpayment.

General Commercial Litigation

The Company, together with a number of other pharmaceutical manufacturers, has been named as a defendant in an action filed in California State Superior Court in Oakland, *James Clayworth et al. v. Bristol-Myers Squibb Company, et al.*, alleging that the defendants have conspired to fix the prices of pharmaceuticals by agreeing to charge more for their drugs in the United States than they charge outside the United States, particularly Canada, and asserting claims under California's Cartwright Act and unfair competition law. The plaintiffs seek treble damages for any damages they have sustained; restitution of any profit obtained by defendants through charging artificially higher prices to plaintiffs; an injunction barring the defendants from charging the plaintiffs higher prices offered to other customers; an award of reasonable attorneys' fees and costs; and any other relief the Court deems proper.

This case is at a preliminary stage, and the Company is unable to assess the outcome and any possible effect on its business and profitability, or reasonably estimate possible loss or range of loss with respect to this case. If the Company were not to prevail in a final, non-appealable determination of this litigation, the impact could be material.

The Company also has been named as a defendant, along with many other pharmaceutical companies, in an action brought by the Utility Consumers Action Network, a consumer advocacy organization that focuses on privacy issues. The lawsuit, filed in California State Superior Court, San Diego County, and entitled *Utility Consumers Action Network on behalf of the Privacy Rights Clearinghouse, et al. v. Bristol-Myers Squibb Co., et al.*, was originally directed only at retail drug stores but was amended in July 2004 to add the Company and the other pharmaceutical companies as defendants. Another lawsuit, *Rowan Klein, a Representative Action on Behalf of Similarly Situated Persons and the Consuming Public, v. Walgreens, et al.*, was filed in February 2005, also in California State Superior Court, San Diego County, against retail pharmacies, the Company and other pharmaceutical companies, and is substantially the same as the Utility Consumers Action Network lawsuit (jointly referred to as "the Complaints"). The Complaints seek equitable relief, monetary damages and attorneys' fees based upon allegedly unfair business practices and untrue and misleading advertising under various California statutes, including the California Confidentiality of Medical Information Act. Specifically, the Complaints allege that through the "Drug Marketing Program", retail stores are selling consumers' confidential medical information to companies. The Complaints further allege that the companies are using consumers' medical information for direct marketing that increase the sale of targeted drugs.

In January 2005, the Company and other pharmaceutical defendants sought to dismiss both the Utility Consumers Action Network case and the Klein case on the grounds that California's Proposition 64 requires that a plaintiff must be the injured party in order to have standing to bring a suit. The Company contends that neither of the plaintiffs in these two cases were personally injured. In October 2005, the Court entered a stay of both cases pending the California Supreme Court's decision to review several intermediate appellate decisions that discuss the applicability of Proposition 64 to pending cases. Both cases are at a very preliminary stage, and the Company is unable to assess the outcome and any possible effect on its business and profitability, or reasonably estimate possible loss or range of loss with respect to this case. If the Company were not to prevail in a final, non-appealable determination of these two lawsuits, the impact could be material.

Product Liability Litigation

The Company is a party to product liability lawsuits involving allegations of injury caused by the Company's pharmaceutical and over-the-counter medications. These lawsuits involve certain over-the-counter medications containing phenylpropanolamine (PPA), while others involve hormone replacement therapy (HRT) products, polyurethane-covered breast implants and smooth-walled breast implants, and the Company's *Serzone* and *Stadol* NS prescription drugs. In addition to lawsuits, the Company also faces unfilled claims involving these and other products.

Serzone. *Serzone* (nefazodone hydrochloride) is an antidepressant that was launched by the Company in May 1994, in Canada and in March 1995, in the United States. In December 2001, the Company added a black box warning to its *Serzone* label warning of the potential risk of severe hepatic events including possible liver failure and the need for transplantation and risk of death. Within several months of the black box warning being added to the package insert for *Serzone*, a number of lawsuits, including several class actions, were filed against the Company. Plaintiffs allege that the Company knew or should have known about the hepatic risks posed by *Serzone* and failed to adequately warn physicians and users of the risks. They seek compensatory and punitive damages, medical monitoring, and refunds for the costs of purchasing *Serzone*. In August 2002, the federal cases were transferred to the U.S. District Court for the Southern District of West Virginia, *In re Serzone Products Liability Litigation*, MDL 1477. In addition to the cases filed in the United States, there are four national class actions filed in Canada. In May 2004, the Company announced that, following an evaluation of the commercial potential of the product after generic entry into the marketplace and rapidly declining brand sales, it had decided to discontinue the manufacture and sale of the product effective June 14, 2004.

Without admitting any wrongdoing or liability, on or around October 15, 2004, the Company entered into a settlement agreement with respect to all claims in the United States and its territories regarding *Serzone*. Pursuant to the terms of the proposed settlement, all claims will be dismissed, the litigation will be terminated, the defendants will receive releases, and the Company commits to paying at least \$70 million to funds for class members. Class Counsel has petitioned the court for an award of reasonable attorneys' fees and expenses; the fees will be paid by the Company and will not reduce the amount of money paid to class members as part of the settlement. The Company may terminate the settlement based upon the number of claims submitted or the number of purported class members who opt not to participate in the settlement and instead pursue individual claims. On November 18, 2004, the District Court conditionally certified the temporary settlement class and preliminarily approved the settlement. The opt-out period ended on April 8, 2005. The fairness hearing occurred on June 29, 2005. On September 2, 2005, the Court issued an opinion granting final approval of the settlement; the order approving the settlement was entered on September 9, 2005.

The Company has reserves for liabilities for these lawsuits of \$76 million, including reasonable attorney's fees and expenses. It is not possible at this time to reasonably assess the final outcome of these lawsuits due to a number of contingencies that could affect the settlement. In accordance with GAAP, the Company has determined that the above amounts represent minimum expected probable losses with respect to these lawsuits. Eventual losses related to these lawsuits may exceed these reserves, and the further impact could be material. The Company does not believe that the top-end of the range for these losses can be estimated.

Hormone Replacement Therapy (HRT) Litigation. In 1991, the National Institutes of Health (NIH) launched the Women's Health Initiative (WHI) clinical trials involving approximately 161,000 healthy, postmenopausal women. The participants were given either Prempro (estrogen and progestin) or Premarin (estrogen), both of which are manufactured by Wyeth. A July 2002, article in the Journal of the American Medical Association reported that among the Prempro subjects, there were increased risks of breast cancer, heart attacks, blood clots and strokes, and decreased risks of hip fractures and colorectal cancer. The Prempro phase of the study was stopped on July 9, 2002. The Premarin phase continued, only to be stopped on March 1, 2004 when the NIH informed study participants that they should stop study medications in the trial of conjugated equine estrogens (Premarin, Estrogen-alone) versus placebo. Women will continue to be followed for several more years, including ascertainment of outcomes and mammogram reports.

The first legal complaints were filed against Wyeth shortly after WHI was halted in July 2002. In July 2003, the Company was served with its first HRT lawsuit. Plaintiffs allege, among other things, that hormone therapy products cause breast cancer, stroke, blood clots, cardiac and other injuries in women, that the defendants were aware of these risks and failed to warn consumers. The Company products involved in this litigation are: Estrace (an estrogen-only tablet); Estradiol (generic estrogen-only tablet); Delestrogen (an injectable estrogen); and Ovcon (an oral contraceptive containing both estrogen and progestin). The federal cases are being transferred to the U.S. District Court for the Eastern District of Arkansas, *In re Prempro (Wyeth) Products Liability Litigation*, MDL No., 1507. As of February 28, 2006, the Company was a defendant in 387 lawsuits involving the above-mentioned products, filed on behalf of approximately 1,012 plaintiffs, in federal and state courts throughout the United States. All of these lawsuits involve multiple defendants. The Company expects to be dismissed from many cases in which its products were never used. All of the Company's hormone therapy products were sold to other companies between January 2000 and August 2001, but the Company maintains the Estrace aNDA, and continues to manufacture some of the products under a supply agreement. It is not possible at this time to reasonably assess the final outcome of this litigation or reasonably estimate possible loss or range of loss with respect to this litigation.

Environmental Proceedings

In October 2005, the Company commenced a voluntary environmental audit of the Mead Johnson facility in Mt. Vernon, Indiana, to determine its compliance with EPA's new source performance standards (NSPS), which are applicable to the operation of an incinerator. In December 2005, the Company disclosed possible violations of the NSPS requirement and is currently in the process of modifying its operations to fall within an exemption from those requirements. To date, neither EPA nor the Indiana Department of Environmental Management have pursued any penalties for these potential violations; however, the Company could potentially be subject to civil penalties for past non-compliance with the NSPS.

The U.S. Environmental Protection Agency (EPA) is investigating industrial and commercial facilities throughout the U.S. that use refrigeration equipment containing ozone-depleting substances (ODS) and enforcing compliance with regulations governing the prevention, service and repair of leaks (ODS requirements). In 2004, the Company performed a voluntary corporate-wide audit at its facilities in the U.S. and Puerto Rico that use ODS-containing refrigeration equipment. The Company submitted an audit report to the EPA in November 2004, identifying potential violations of the ODS requirements at several of its facilities. In addition to the matters covered in the Company's audit report letter to the EPA, the EPA previously sent the Company's wholly owned subsidiary, Mead Johnson, a request for information regarding compliance with ODS requirements at its facility in Evansville, Indiana. The Company responded to the request in June 2004, and, as a result, identified potential violations at the Evansville facility. The company currently is in discussions with EPA to resolve both the potential violations discovered during the audit and those identified as a result of the EPA request for information to the Evansville facility. If the EPA determines that the Evansville facility, or any other facilities, was, or is, in violation of applicable ODS requirements, the Company could be subject to penalties and/or be required to convert or replace refrigeration equipment to use non-ODS approved substitutes.

In March 2005, the Company commenced a voluntary environmental audit of the Barceloneta and Humacao, Puerto Rico, facilities to determine their compliance with EPA's regulations regarding the maximum achievable control technology requirements for emissions of hazardous air pollutants from pharmaceuticals production (Pharmaceutical MACT). The Company submitted to EPA an audit report for the Humacao facility in June 2005 and for the Barceloneta facility in July 2005, which disclosed potential violations of the Pharmaceutical MACT requirements at both facilities. To date, EPA has not discussed these potential violations with the Company; however, the Company is undertaking actions to correct the potential violations. If EPA determines that the Barceloneta and Humacao facilities violated the Pharmaceutical MACT requirements, the Company could be subject to civil penalties and/or be required to make investments in the facilities to ensure their compliance with the Pharmaceutical MACT.

In October 2003, the Company was contacted by the North Brunswick, NJ Board of Education (BOE) regarding the discovery of industrial waste materials allegedly including materials from E.R. Squibb and Sons during an expansion project at the North Brunswick Township High School, as well as at a number of neighboring residential properties and adjacent public park areas. In January 2004, the New Jersey Department of Environmental Protection (NJDEP) sent the Company and others an information request letter about possible waste disposal at the site, to which the Company responded in March 2004. The school board and the Township, who are the current owners of the school property and the park, are conducting and jointly financing soil remediation work under a work plan approved by the NJDEP, and are evaluating the need to conduct response actions to remediate or contain potentially impacted ground water. Due to financial constraints, the BOE has asked the Company to contribute funds on an interim basis to assure uninterrupted performance of necessary site work. The Company is actively monitoring the clean-up project, including its costs, and has offered to negotiate with the BOE and Township on the terms of a cooperative funding agreement and allocation process. Municipal records indicate the Township operated a landfill at the site in the 1940's through the 1960's, and the Company is actively investigating the historic use of the site, including the Company's possible connection. To date, neither the BOE or the Township have asserted any claims against the Company.

In September 2003, the NJDEP issued an administrative enforcement Directive and Notice under the New Jersey Spill Compensation and Control Act requiring the Company and approximately 65 other companies to perform an assessment of natural resource damages (NRD) and to implement unspecified interim remedial measures to restore conditions in the Lower Passaic River. The Directive alleges that the Company is liable because it historically sent bulk waste to the former Inland Chemical Company facility in Newark, N.J. (now owned by McKesson Corp.) for reprocessing, and that releases of hazardous substances from this facility have migrated into Newark Bay and continue to have an adverse impact on the Lower Passaic River watershed. Subsequently, the EPA also issued a notice letter under the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) to numerous parties—but not including the Company—seeking their cooperation in a study of conditions in substantially the same stretch of the Passaic River that is the subject of the NJDEP's Directive. A group of these other parties entered into a consent agreement with EPA in 2004 to finance a portion of that study. The EPA initially estimated this study to cost \$20 million, but recent EPA internal estimates have pegged the number at least twice that amount. Under the consent agreement, the private party group has committed to pay roughly half of the \$20 million estimate, subject to revision and future negotiation. This study may also lead to clean-up actions, directed by the EPA and the Army Corps of Engineers. The Company is working cooperatively with a group of the parties that received the NJDEP Directive and/or the EPA notice to explore potential resolutions of the Directive and to address the risk of collateral claims. Although the Company does not believe it has caused or contributed to any contamination in the Lower Passaic River watershed, the Company has informed the NJDEP that it is willing to discuss the NJDEP's allegations against the Company. Also, the private party group continues to discuss with the federal agencies designated as trustees of natural resources affected by contamination in the Passaic River watershed the possibility of funding a cooperative NRD study that presumably would dovetail with the ongoing EPA study, and ideally would be joined by the NJDEP, to coordinate actions NJDEP may seek under the Directive. In late 2005, the NJDEP issued a supplemental Directive and filed suit against one of the site parties, seeking to compel implementation of interim measures. It is unclear whether the NJDEP will take additional actions against other site parties and/or whether litigation will arise in response to these new claims. The extent of any liability the Company may face, either to NJDEP or EPA, or with respect to future claims by the federal trustees, McKesson or other responsible parties, cannot yet be determined.

On December 1, 2003, the Company and the NJDEP entered an Administrative Consent Order (ACO) concerning alleged violations of the New Jersey Air Pollution Control Act and its implementing regulations at the Company's New Brunswick facility. Pursuant to the ACO, the Company agreed to submit a permit application creating a facility-wide emissions cap and to pay a small administrative fine. Both of these obligations were satisfied in early 2004. Subsequently, on February 15, 2005, the ACO was amended to provide that the Company would install a new cogeneration turbine at its New Brunswick facility by December 31, 2006, and would obtain applicable air permits by December 31, 2005. The Company obtained the applicable permits and is purchasing the new cogeneration turbine at a cost of approximately \$5 million.

The Company is one of several defendants, including most of the major U.S. pharmaceutical companies, in a purported class action suit filed in superior court in Puerto Rico in February 2000 by residents of three wards from the Municipality of Barceloneta, alleging that air emissions from a government owned and operated wastewater treatment facility in the Municipality have caused respiratory and other ailments, violated local air rules and adversely impacted property values. The Company believes its wastewater discharges to the treatment facility are in material compliance with the terms of the Company's permit. In September 2005 the parties stipulated to the dismissal (with prejudice) of all claims for property damage and personal injury, leaving only claims related to nuisance remaining in the case. The court had scheduled a hearing on the class certification motion for September 30, 2005, but that hearing was adjourned. Settlement discussions among the parties continued in November and December but were not successful. In February 2006, a new judge was appointed due to a potential conflict of interest involving the prior judge and a case status conference is scheduled for April 2006. The Company believes that this litigation will be resolved for an immaterial amount, which may bring the matter to resolution. However, in the event of an adverse judgment, the Company's ultimate financial liability could be greater than anticipated.

The Company is also responsible under various state, federal and foreign laws, including CERCLA, for certain costs of investigating and/or remediating contamination resulting from past industrial activity at the Company's current or former sites or at waste disposal or reprocessing facilities operated by third parties. The Company typically estimates these costs based on information obtained from the EPA, or counterpart state agency, and/or studies prepared by independent consultants, including the total estimated costs for the site and the expected cost-sharing, if any, with other "potentially responsible parties." The Company accrues liabilities when they are probable and reasonably estimable. As of December 31, 2005, the Company estimated its share of the total future costs for these sites to be approximately \$68.5 million, recorded as other liabilities, which represents the sum of best estimates or, where no simple estimate can reasonably be made, estimates of the minimal probable amount among a range of such costs (without taking into account any potential recoveries from other parties, which are not currently expected). The Company has paid less than \$4 million (excluding legal fees) in each of the last five years for investigation and remediation of such matters, including liabilities under CERCLA and for other on-site remedial obligations. Although it is not possible to predict with certainty the outcome of these environmental proceedings or the ultimate costs of remediation, the Company does not believe that any reasonably possible expenditures that the Company may incur in excess of existing reserves will have a material adverse effect on its business, financial position, or results of operations.

Other Matters

On October 25, 2004, the SEC notified the Company that it is conducting an informal inquiry into the activities of certain of the Company's German pharmaceutical subsidiaries and its employees and/or agents. The SEC's informal inquiry encompasses matters currently under investigation by the German prosecutor in Munich, Germany. The Company understands the inquiry and investigation concern potential violations of the Foreign Corrupt Practices Act and German law. The Company is cooperating with both the SEC and the German authorities. The Company has established an accrual which represents minimum expected probable losses with respect to the investigation by the German prosecutor.

In January 2006, the Company was notified by the Prosecutor in the Bari region of Italy ("Prosecutor") that the Company is under investigation as a result of the activities of two of its employees in the region. The investigation involves the Company, as well as a number of doctors, pharmacists, pharmaceutical companies and their sales representatives. The main allegation is that the parties were engaged in a plan to defraud the National Health Service. The Prosecutor also alleges that the companies lacked appropriate compliance controls and/or processes and procedures to control the activities of their sales representatives. A hearing is scheduled for March 23, 2006 on the Prosecutor's request to close the operations of the pharmaceutical companies under investigation and to appoint a judicial administrator as preliminary measures. The Company believes the request is unwarranted.

Indemnification of Officers and Directors

The Company's corporate by-laws require that, to the extent permitted by law, the Company shall indemnify its officers and directors against judgments, fines, penalties and amounts paid in settlement, including legal fees and all appeals, incurred in connection with civil or criminal actions or proceedings, as it relates to their services to the Company and its subsidiaries. The by-laws provide no limit on the amount of indemnification. Indemnification is not permitted in the case of willful misconduct, knowing violation of criminal law, or improper personal benefit. As permitted under the laws of the state of Delaware, the Company has for many years purchased directors' and officers' insurance coverage to cover claims made against the directors and officers. The amounts and types of coverage have varied from period to period as dictated by market conditions.

The litigation matters and regulatory actions described above involve certain of the Company's current and former directors and officers, all of whom are covered by the aforementioned indemnity and if applicable, certain prior period insurance policies. However, certain indemnification payments may not be covered under the Company's directors' and officers' insurance coverage. The Company cannot predict with certainty the extent to which the Company will recover from its insurers the indemnification payments made in connection with the litigation matters and regulatory actions described above.

Note 21 Subsequent Events

In January 2006, the Company completed the sale of its inventory, trademark, patent and intellectual property rights related to Dovonex, a treatment for psoriasis in the United States, to Warner Chilcott Company, Inc. for \$200 million in cash. In addition, the Company will receive a royalty based on 5% of net sales of Dovonex through the end of 2007. As a result of this transaction, the Company expects to recognize a pre-tax gain of approximately \$200 million (\$126 million net of tax) in the first quarter of 2006, subject to certain post-closing adjustments.

Note 22 Selected Quarterly Financial Data (Unaudited)

Dollars in Millions, Except Per Share Data	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
2005:					
Net Sales	\$ 4,532	\$ 4,889	\$ 4,767	\$ 5,019	\$ 19,207
Gross Margin	3,165	3,406	3,284	3,424	13,279
Earnings from Continuing Operations ⁽¹⁾	538	991	964	499	2,992
Discontinued Operations, net	(5)	13	—	—	8
Net Earnings	533	1,004	964	499	3,000
Earnings per common share:					
Basic					
Earnings from Continuing Operations ⁽¹⁾	\$ 0.27	\$ 0.51	\$ 0.49	\$ 0.26	\$ 1.53
Discontinued Operations, net	—	—	—	—	—
Net Earnings	\$ 0.27	\$ 0.51	\$ 0.49	\$ 0.26	\$ 1.53
Diluted ⁽³⁾					
Earnings from Continuing Operations ⁽¹⁾	\$ 0.27	\$ 0.50	\$ 0.49	\$ 0.26	\$ 1.52
Discontinued Operations, net	—	—	—	—	—
Net Earnings	\$ 0.27	\$ 0.50	\$ 0.49	\$ 0.26	\$ 1.52
Dividends declared per Common Share	\$ 0.28	\$ 0.28	\$ 0.28	\$ 0.28	\$ 1.12
Cash and cash equivalents	\$ 3,311	\$ 1,798	\$ 2,129	\$ 3,050	\$ 3,050
Marketable securities	2,671	1,242	1,652	2,749	2,749
2004:					
Net Sales	\$ 4,626	\$ 4,819	\$ 4,778	\$ 5,157	\$ 19,380
Gross Margin	3,269	3,320	3,310	3,492	13,391
Earnings from Continuing Operations ⁽²⁾	961	523	755	139	2,378
Discontinued Operations, net	3	4	3	—	10
Net Earnings	964	527	758	139	2,388
Earnings per common share:					
Basic					
Earnings from Continuing Operations ⁽²⁾	\$ 0.50	\$ 0.27	\$ 0.39	\$ 0.07	\$ 1.23
Discontinued Operations, net	—	—	—	—	—
Net Earnings	\$ 0.50	\$ 0.27	\$ 0.39	\$ 0.07	\$ 1.23
Diluted ⁽³⁾					
Earnings from Continuing Operations ⁽²⁾	\$ 0.49	\$ 0.27	\$ 0.38	\$ 0.07	\$ 1.21
Discontinued Operations, net	—	—	—	—	—
Net Earnings	\$ 0.49	\$ 0.27	\$ 0.38	\$ 0.07	\$ 1.21
Dividends declared per Common Share	\$ 0.28	\$ 0.28	\$ 0.28	\$ 0.28	\$ 1.12
Cash and cash equivalents	\$ 3,173	\$ 3,227	\$ 3,446	\$ 3,680	\$ 3,680
Marketable securities	3,552	3,686	3,872	3,794	3,794

Note: Earnings per share for the quarters may not add to the amounts for the year, as each period is computed on a discrete basis.

⁽¹⁾ 2005 includes litigation charges of \$124 million, \$269 million and \$197 million in the first, second and fourth quarters, respectively. The second and third quarters include litigation insurance recoveries of \$295 million and \$26 million, respectively. The first, second, third and fourth quarters include restructuring and other items of \$17 million, \$24 million, \$30 million and \$86 million, respectively. The first and fourth quarters include upfront payments for licensing agreements of \$35 million and \$9 million, respectively. The first and second quarters include \$18 million and \$9 million, respectively, from the gain on sale of equity investments. The first, second and third quarters include \$16 million, \$1 million and \$1 million, respectively, from the loss on sale of fixed assets. The second quarter includes debt retirement costs of \$69 million. The fourth quarter includes \$138 million deferred income, net of costs resulting from the termination of the collaborative agreement with Merck for muraglitazar. The third quarter includes the gain on sale of the Consumer Medicines business of \$569 million.

⁽²⁾ 2004 includes litigation charges of \$480 million, \$36 million and \$16 million in the second, third, and fourth quarters, respectively. The second quarter includes litigation settlement income of \$25 million. The first, second, third, and fourth quarters include the gain on the sale of the Adult Nutritional business of \$295 million, \$18 million, \$3 million, and \$4 million, respectively. The first, second, third, and fourth quarters include provisions for restructuring and other items of \$29 million, \$17 million, \$105 million, and \$61 million, respectively. The first, second, third, and fourth quarters include upfront payments for licensing agreements of \$5 million, \$25 million, \$10 million, and \$15 million, respectively. The second and third quarters include write-offs for acquired in-process research and development of \$62 million and \$1 million, respectively.

⁽³⁾ Common equivalent shares excluded from the computation of diluted earnings per share, because the effect would be anti-dilutive, were as follows (in millions):

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
2005	142	141	139	156	156
2004	133	130	129	126	126

Reports of Management

Management's Responsibility for Financial Statements

Management is responsible for the preparation and integrity of the financial information presented in this Annual Report. The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP), applying certain estimates and judgments as required. In management's opinion, the consolidated financial statements present fairly the Company's financial position, results of operations and cash flows.

The Audit Committee of the Board of Directors meets regularly with the internal auditors, PricewaterhouseCoopers LLP (PwC), the Company's independent registered accounting firm, and management to review accounting, internal control structure and financial reporting matters. The internal auditors and PwC have full and free access to the Audit Committee. As set forth in the Company's Standard of Business Conduct and Ethics, the Company is firmly committed to adhering to the highest standards of moral and ethical behavior in all of its business activities.

Management's Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Under the supervision and with the participation of management, including the chief executive officer and chief financial officer, management assessed the effectiveness of internal control over financial reporting as of December 31, 2005 based on the framework in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on that assessment, management has concluded that the Company's internal control over financial reporting was effective at December 31, 2005 to provide reasonable assurance regarding the reliability of its financial reporting and the preparation of its financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America (GAAP). Due to its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PricewaterhouseCoopers LLP, an independent registered public accounting firm, has audited the Company's consolidated financial statements included in this Annual Report and has issued its report on management's assessment of the effectiveness of the Company's internal control, which appears on page 116 in this Annual Report.



Peter R. Dolan
Chief Executive Officer



Andrew R.J. Bonfield
Chief Financial Officer

March 13, 2006

Report of Independent Registered Public Accounting Firm

To the Board of Directors
and Stockholders of
Bristol-Myers Squibb Company:

We have completed integrated audits of Bristol-Myers Squibb Company's 2005 and 2004 consolidated financial statements and of its internal control over financial reporting as of December 31, 2005, and an audit of its December 31, 2003 consolidated financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Our opinions, based on our audits, are presented below.

Consolidated financial statements

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of earnings, comprehensive income and retained earnings and of cash flows present fairly, in all material respects, the financial position of Bristol-Myers Squibb Company and its subsidiaries at December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2005 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Internal control over financial reporting

Also, in our opinion, management's assessment, included in Management's Report on Internal Control Over Financial Reporting appearing on page 115 in this Annual Report, that the Company maintained effective internal control over financial reporting as of December 31, 2005 based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), is fairly stated, in all material respects, based on those criteria. Furthermore, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control—Integrated Framework* issued by the COSO. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express opinions on management's assessment and on the effectiveness of the Company's internal control over financial reporting based on our audit. We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

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

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



PricewaterhouseCoopers LLP
Philadelphia, PA
March 13, 2006

Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of December 31, 2005, management carried out an evaluation, under the supervision and with the participation of its chief executive officer and chief financial officer, of the effectiveness of the design and operation of its disclosure controls and procedures as such term is defined under Exchange Act Rule 13a-15(e). Based on this evaluation, management has concluded that as of December 31, 2005, such disclosure controls and procedures were effective to provide reasonable assurance that the Company records, processes, summarizes and reports the information the Company must disclose in reports that the Company files or submits under the Securities Exchange Act of 1934, as amended, within the time periods specified in the SEC's rules and forms.

Management's Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Under the supervision and with the participation of management, including the chief executive officer and chief financial officer, management assessed the effectiveness of internal control over financial reporting as of December 31, 2005 based on the framework in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on that assessment, management has concluded that the Company's internal control over financial reporting was effective at December 31, 2005 to provide reasonable assurance regarding the reliability of its financial reporting and the preparation of its financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America (GAAP). Due to its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PricewaterhouseCoopers LLP, an independent registered public accounting firm, has audited the Company's consolidated financial statements included in this Annual Report and has issued its report on management's assessment of the effectiveness of the Company's internal control, which appears on page 116 in this Annual Report.

Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting during the quarter ended December 31, 2005 that have materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Five-Year Financial Summary

Amounts in Millions, Except Per Share Data	2005	2004	2003	2002	2001
Income Statement Data: ⁽¹⁾⁽²⁾					
Net Sales	\$ 19,207	\$ 19,380	\$ 18,653	\$ 16,208	\$ 16,612
Earnings from Continuing Operations Before Minority Interest and Income Taxes	4,516	4,418	4,680	2,748	2,252
Earnings from Continuing Operations	2,992	2,378	3,097	2,059	1,866
Earnings from Continuing Operations per Common Share:					
Basic	\$ 1.53	\$ 1.23	\$ 1.60	\$ 1.07	\$.96
Diluted	\$ 1.52	\$ 1.21	\$ 1.59	\$ 1.06	\$.95
Average common shares outstanding:					
Basic	1,952	1,942	1,937	1,936	1,940
Diluted	1,983	1,976	1,950	1,942	1,965
Dividends paid on common and preferred stock	\$ 2,186	\$ 2,174	\$ 2,169	\$ 2,168	\$ 2,137
Dividends declared per Common Share	\$ 1.12	\$ 1.12	\$ 1.12	\$ 1.12	\$ 1.11
Financial Position Data at December 31: ⁽³⁾					
Total Assets	\$ 28,138	\$ 30,435	\$ 27,448	\$ 25,106	\$ 27,864
Cash and cash equivalents	3,050	3,680	2,549	2,451	4,552
Marketable securities	2,749	3,794	3,013	1,622	1,102
Long-term debt	8,364	8,463	8,522	6,261	6,237
Stockholders' Equity	11,208	10,202	9,786	8,756	8,762

⁽¹⁾ The Company recorded items that affected the comparability of results, which are set forth in the table under Management's Discussion and Analysis of Financial Condition and Results of Operations—Expenses for the years 2005, 2004 and 2003. For a discussion of these items, see Management's Discussion and Analysis of Financial Condition and Results of Operations—Expenses, Note 2 "Alliances and Investments"; Note 3 "Restructuring and Other Items"; Note 4 "Acquisitions and Divestitures"; Note 5 "Discontinued Operations"; and Note 20 "Legal Proceedings and Contingencies."

⁽²⁾ Excludes discontinued operations of OTN in all years; and Clairol and Zimmer in 2001 and 2002.

⁽³⁾ Includes discontinued operations for years 2001 through 2004.

Board of Directors and Management Executive Committee

Board of Directors

James D. Robinson III

Non-Executive Chairman, Bristol-Myers Squibb, and General Partner and Cofounder, RRE Ventures (d)

Robert E. Allen

Retired Chairman and Chief Executive Officer, AT&T Corporation (a,b,d)

Lewis B. Campbell

Chairman, President and Chief Executive Officer, Textron Inc. (a,b,c)

Vance D. Coffman

Retired Chairman and Chief Executive Officer, Lockheed Martin Corporation (a,c)

James M. Cornelius

Chairman and Chief Executive Officer, Guidant Corporation (a,c)

Peter R. Dolan

Chief Executive Officer, Bristol-Myers Squibb (d)

Louis J. Freeh

Former Vice Chairman and General Counsel, MBNA America Bank, N.A. (a,b)

Louis V. Gerstner, Jr.

Retired Chairman and Chief Executive Officer, IBM Corporation (b,d)

Laurie H. Glimcher, M.D.

Irene Heinz Given Professor of Immunology, Harvard School of Public Health, and Professor of Medicine, Harvard Medical School (a,b)

Leif Johansson

President, AB Volvo, and Chief Executive Officer, The Volvo Group (a,b)

Louis W. Sullivan, M.D.

President Emeritus, Morehouse School of Medicine (a,c)

(a) Audit Committee

(b) Committee on Directors and Corporate Governance

(c) Compensation and Management Development Committee

(d) Executive Committee

Management Executive Committee

Peter R. Dolan

Chief Executive Officer

Lamberto Andreotti

Executive Vice President and President, Worldwide Pharmaceuticals

Stephen E. Bear

Senior Vice President, Human Resources

Andrew G. Bodnar, M.D.

Senior Vice President, Strategy and Medical and External Affairs

Andrew R.J. Bonfield

Chief Financial Officer

John E. Celentano

President, Health Care Group

Carlo de Notaristefani, CIRM

President, Technical Operations

Wendy L. Dixon, Ph.D.

President, Global Marketing, and Chief Marketing Officer

Anthony C. Hooper

President, U.S. Pharmaceuticals

Tamar D. Howson

Senior Vice President, Corporate and Business Development

John L. McGoldrick

Executive Vice President

Susan P. O'Day

Chief Information Officer and Vice President, Global Shared Services

Elliott Sigal, M.D., Ph.D.

Chief Scientific Officer and President, Pharmaceutical Research Institute

Jonathan K. Sprole

Chief Compliance Officer and Vice President and Deputy General Counsel

Richard K. Willard

Senior Vice President and General Counsel

Richard L. Wolgemuth, Ph.D.

Senior Vice President, Global Regulatory Sciences

David L. Zabor

Vice President, Strategic Business Initiatives

Robert T. Zito

Senior Vice President, Corporate and Business Communications, and Chief Communications Officer

Stockholder Information

Common Stock

Ticker symbol: BMJ
New York Stock Exchange
Pacific Stock Exchange

Annual Meeting of Stockholders

Tuesday, May 2, 2006
10:00 a.m., Hotel duPont
11th and Market Streets
Wilmington, DE 19801

Stockholder Services and Programs

All inquiries concerning stockholder accounts and stock transfer matters including address changes, the elimination of duplicate mailings, dividend reinvestment (see next column) and direct deposit of dividends should be directed to the Company's Transfer Agent and Registrar:

Mellon Investor Services

P.O. Box 3316
South Hackensack, NJ 07606
www.melloninvestor.com
800-356-2026 (within the U.S.)
201-680-6578 (outside the U.S.)
TDD telephone service for the hearing-impaired:
800-231-5469 (within the U.S.)
201-680-6610 (outside the U.S.)

Dividend Reinvestment Plan

Registered stockholders (stock must be held in your name) who hold 50 or more shares of the Company's stock may participate in its stockholder-paid Dividend Reinvestment Plan (DRIP), which includes a safekeeping and sale-of-stock feature. If you hold fewer than 50 shares, you are still eligible to participate in the safekeeping and sale-of-stock features as well as the direct registration option.

Form 10-K

For a free copy of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005, contact:
Secretary
Bristol-Myers Squibb Company
345 Park Avenue
New York, NY 10154-0037

Form 10-K is also available at
www.bms.com/investors

The most recent certifications by the Company's chief executive officer and chief financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 are filed as exhibits to the Company's Form 10-K. The Company has also filed with the New York Stock Exchange the most recent Annual CEO Certification as required by Section 303A.12(a) of the New York Stock Exchange Listed Company Manual.

The following reports are available by writing to:

Corporate and Business Communications
Bristol-Myers Squibb Company
345 Park Avenue
New York, NY 10154-0037

- Bristol-Myers Squibb Foundation
- Sustainability/Environmental Programs
- Political Contributions
- EEO-1 Report

This Annual Report contains certain forward-looking information within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements involve substantial risks and uncertainties that could cause actual results to differ materially from the expectations or estimates reflected in the forward-looking statements. Please see page 71 for a discussion and description of these risks and uncertainties. The company undertakes no obligation to publicly update any forward-looking statement, whether as a result of new information, future events or otherwise.

Product Names and Company Programs

appearing throughout in italics are trademarks of Bristol-Myers Squibb Company or one of its subsidiary companies. Global products are referred to herein by their registered and approved U.S. trademarks, unless specifically noted otherwise.

Abilify is a trademark of Otsuka Pharmaceutical Company, Ltd.

Avapro, Avalide, Aprovel, Karvea, Karvezide, Plavix and Iscover are trademarks of Sanofi-Aventis.

Bufferin and Excedrin are trademarks of Novartis AG.

Delestrogen is a trademark of Jones Pharma, Inc.

Dovonex is a trademark of Leo Pharma A/S.

EMSAM is a trademark of Somerset Pharmaceuticals, Inc.

Erbix is a trademark of ImClone Systems Incorporated.

Estrace and Ovcon are trademarks of Warner Chilcott Company, Inc.

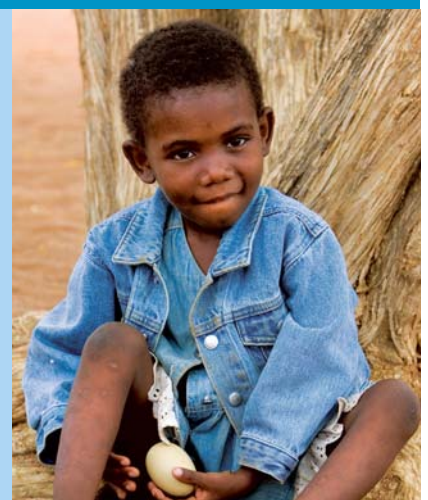
Glucophage IR, Glucophage XR, Glucovance, and Metaglip are trademarks of Merck Santé S.A.S., an associate of Merck KGaA of Darmstadt, Germany.

Premarin and Prempro are trademarks of Wyeth.

Truvada is a trademark of Gilead Sciences, Inc.

On the back cover

MOGODITSHANE, BOTSWANA In Africa, HIV/AIDS strikes the most vulnerable. Kagiso, a five-year-old girl with wistful eyes and a shy smile, is one such victim. She is being raised by her aunt along with 11 other orphans in a four room house. In March 2005, Kagiso was near death with full-blown AIDS and tuberculosis. Today, thanks to the nurses and doctors at the Botswana-Baylor Children's Clinical Center of Excellence—funded by Bristol-Myers Squibb—Kagiso runs and plays like other children.



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Designed, written and photographed by the Bristol-Myers Squibb Corporate and Business Communications Department.

 Printed on recycled paper: cover and text, 10% post-consumer waste; financial review, 30% post-consumer waste.



Bristol-Myers Squibb