CHIRON CORP
Form 10-K
March 16, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark one)

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the fiscal year ended December 31, 2005

OR

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

For the transition period from to

Commission File Number: 0-12798

CHIRON CORPORATION

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**94-2754624**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
4560 Horton Street, Emeryville, California	**94608**
(Address of Principal Executive Offices)	(Zip Code)

Registrant s Telephone Number, Including Area Code: **(510) 655-8730**

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

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, $0.01 Par Value

Warrant to Purchase Common Stock, $0.01 Par Value

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes: x No: o

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

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

Large accelerated filer x	Accelerated filer o	Non-accelerated filer o

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

The aggregate market value of the voting and non-voting stock held by non-affiliates of the registrant, based upon the closing price of Common Stock on June 30, 2005 as reported on the NASDAQ National Market, was approximately $2.9 billion. Shares of Common Stock held by each executive officer and director and by each shareholder whose beneficial ownership exceeds 5% of the outstanding Common Stock at June 30, 2005 have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

The aggregate market value of voting and non-voting stock held by non-affiliates of the registrant as of January 31, 2006 was $3.4 billion. The number of shares outstanding of each of the registrant s classes of common stock as of January 31, 2006:

Title of Class	**Number of shares**
Common Stock, $0.01 par value	197,154,517

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement to be filed in connection with the solicitation of proxies for the Annual Meeting of Stockholders to be held on June 22, 2006 are incorporated by reference into Part III of this Report.

PART I

ITEM 1. BUSINESS

Our Policy on Forward-Looking Statements

This 10-K contains forward-looking statements regarding our expectations, hopes or intentions regarding the future, including statements relating to sales growth, product development initiatives, regulatory approval, new product marketing, acquisitions, litigation, competition, and licensing activities that involve risks and uncertainties and are subject to change. The forward-looking statements contained in this 10-K reflect our current expectations on the date of this 10-K. Actual results, performance or outcomes may differ materially from current expectations. Our actual performance may differ from current expectations due to many factors, including additional adverse developments resulting from the suspension from October 5, 2004 through March 2, 2005 of Chiron s UK license to manufacture FLUVIRIN® influenza virus vaccine, the announcement of such suspension and the litigation and investigations relating to these matters, the outcome of clinical trials, regulatory review and approvals, remediation activities, manufacturing capabilities, intellectual property protections and defenses, stock price volatility and marketing effectiveness. In particular there can be no assurance that we will increase sales of existing products, successfully develop and receive approval to market new products, or achieve market acceptance for such new products. No assurances can be given that the transaction contemplated by the merger agreement with Novartis AG will be consummated. In addition, we may engage in business opportunities, the successful completion of which is subject to certain risks, including approval by Novartis, other stockholders, regulatory approvals and the integration of operations. We have discussed the important factors that we believe could cause actual results to differ from what is expressed in the forward-looking statements, in Part II, Item 7, of this 10-K, Management s Discussion and Analysis of Financial Condition and Results of Operations, under the caption Factors That May Affect Future Results. We do not undertake an obligation to update the forward-looking information contained in this 10-K.

Overview

We are a global biopharmaceutical company that participates in three healthcare markets: blood testing, vaccines, and biopharmaceuticals. Our revenues, which totaled $1.9 billion in 2005, consist of product sales, revenues from a joint business contractual arrangement, collaborative agreement revenues, royalty and license fee revenues and other revenues, primarily consisting of contract manufacturing and grant revenues. Our research and development efforts are focused on developing products for oncology and infectious and pulmonary disease.

Blood Testing

Our Blood Testing segment is dedicated to improving blood safety through the development and sale of novel blood-screening assays and equipment that protect the world s blood supply. Our Blood Testing segment, which reported total revenues of $555.7 million in 2005, is a world leader in nucleic acid testing, or NAT, blood screening with a leading position in the U.S, and a strong presence in Europe and Asia. The segment also generates revenues from a joint business contractual arrangement, a collaboration agreement, royalties and license fees.

Our Blood Testing segment consists of two separate collaborations: an alliance with Gen-Probe Incorporated (Gen-Probe) for NAT products, and a joint business contractual arrangement with Ortho-Clinical Diagnostics, Inc. (Ortho-Clinical Diagnostics) for immunodiagnostic products. Our collaboration with Gen-Probe was formed in 1998 and focuses on developing and commercializing NAT products to screen donated blood, plasma, organs and tissue for viral infection. We sell the collaboration s assays and instruments to blood banks under the PROCLEIX® brand name. Our joint business contractual arrangement with Ortho-Clinical Diagnostics was formed in 1989 to develop and sell immunodiagnostic

tests to detect retroviruses and hepatitis viruses in blood. Ortho-Clinical Diagnostics manufactures and sells the assays and instrument systems. Chiron shares equally in the profit of the contractual arrangement. Our Blood Testing segment also earns royalties and license fees from third parties based on their sales of immunodiagnostic and nucleic acid testing probe diagnostic products utilizing our hepatitis C virus and HIV-related patents, for use in blood screening and plasma fractionation markets.

Research and development is focused on programs to improve blood safety, including the development of an enzyme conversion system that converts groups A, B and AB red blood cells to enzyme-converted universal blood group O, and the development of a blood-screening assay for variant Creutzfeldt-Jakob disease (vCJD).

Vaccines

Our vaccines segment is the fifth largest vaccines business in the world with total revenues of $602.1 million in 2005. We offer approximately 20 pediatric and adult vaccines including influenza, meningococcal, travel and pediatric vaccines. These vaccines have protected millions of people globally from potentially fatal diseases such as influenza, polio, rabies and meningococcal disease. We market our vaccines primarily in the United States, Germany, Italy and the United Kingdom.

Our heritage in vaccines is traced to the three European manufacturers we acquired over the past two decades, all of which were originally founded 100 or more years ago: Italy-based Sclavo was acquired in 1992, Germany-based Behring was acquired in 1998 and United Kingdom-based PowderJect Pharmaceutical plc, or PowderJect, was acquired in July 2003. We acquired FLUVIRIN® influenza virus vaccine as part of our acquisition of PowderJect.

Our vaccines segment research and development is focused on developing next generation influenza manufacturing capability, including our cell culture derived influenza vaccine, developing new vaccines for pandemic preparedness, and broadening our meningococcal franchise.

Biopharmaceuticals

Our biopharmaceuticals segment researches, develops, manufactures and markets a range of therapeutic products for cancer and infectious and pulmonary disease. The biopharmaceutical segment, which includes both product sales and royalties, reported total revenues of $629.0 million for the year 2005. Our marketed products include TOBI® tobramycin solution for inhalation, USP for pseudomonal lung infections in cystic fibrosis patients; PROLEUKIN® (aldesleukin) for injection for metastatic melanoma and renal cell carcinoma; and BETASERON® (interferon beta-1b) for subcutaneous injection for multiple sclerosis. In January 2006, the European Commission granted marketing approval to Chiron for CUBICIN® (daptomycin), a first-in-class IV antibiotic, adding another commercial product to our portfolio. The marketing approval was granted in the 25 member states of the European Union, Iceland, Liechtenstein and Norway. Under the approval, CUBICIN® is indicated for the treatment of complicated skin and soft-tissue infections (cSSTI) caused by Gram-positive bacteria. Research and development efforts are focused in the areas of oncology and infectious and pulmonary disease including the development of tobramycin inhalation powder, or TIP, a new tobramycin product with an enhanced method of delivery and the clinical advancement of tifacogin for the treatment of severe community-acquired pneumonia. Our oncology pipeline includes CHIR-258, a growth factor kinase inhibitor, CHIR-12.12, an anti CD-40 monoclonal antibody and CHIR-265, a Raf kinase inhibitor.

Royalties and License Fee Revenue

We earn royalty and license fee revenue in all three segments by licensing some of our key intellectual property in areas such as hepatitis C and HIV. In addition, we generate royalties through agreements with development and marketing partners, including royalties from Schering AG s sales of BETAFERON®

(interferon beta-1b) for SC injection in Europe. Some royalties and license fees are not considered to be associated with any particular business segment and are recorded separately in the segment data as Other Royalty and License Fee Revenues. Financial information for the reportable segments is included in Note 18, Segment Information of Notes to Consolidated Financial Statements.

We were incorporated in California in 1981 and merged into a Delaware corporation in November 1986. Our principal executive offices are located at 4560 Horton Street, Emeryville, California 94608, and our main telephone number is (510) 655-8730.

Product Descriptions

Blood Testing

Our collaboration with Gen-Probe is focused on developing and commercializing NAT products using transcription-mediated amplification, or TMA, technology to screen donated blood, plasma, organs and tissue for viral infection. Compared to immunodiagnostic testing, where infection is determined by the presence of antibodies, testing directly for the presence of viral nucleic acids improves the sensitivity of testing and enables infection to be detected earlier than with previously approved technologies.

We sell assays and instrumentation under the PROCLEIX® brand name, and Gen-Probe receives a percentage of our sales revenues. Under the terms of the collaboration agreement, Gen-Probe performs certain product development and manufacturing functions, while Chiron and Gen-Probe jointly participate in new assay and instrument research and development.

Assays developed with Gen-Probe, and their status in the United States and the rest of world include:

	U.S.	**Ex-U.S.**
PROCLEIX® HIV-1/HCV Assay	Marketed	Marketed
PROCLEIX® WNV Assay (West Nile Virus)	Marketed	N/A
PROCLEIX® ULTRIO® Assay (HIV-1, HCV, and HBV)	Biologics License Application filed	Marketed

The PROCLEIX® HIV-1/HCV Assay is a NAT product that was co-developed with Gen-Probe for the simultaneous detection of HIV-1 and hepatitis C virus (HCV) in plasma, whole blood, organs and tissue donations. The global need for HIV-1 and HCV testing continues to increase. Last year, approximately 5 million people acquired HIV, bringing the number of people in the world living with HIV to 39 million, the highest level ever. Annually, approximately 3 million people die from AIDS, the disease caused by HIV infection. HCV is a major cause of acute hepatitis and chronic liver disease, including cirrhosis and liver cancer. Globally, an estimated 170 million persons are chronically infected with HCV and 3 to 4 million persons are newly infected each year. The major causes of HCV infection worldwide are use of unscreened blood transfusions, and re-use of needles and syringes that have not been adequately sterilized. The PROCLEIX® HIV-1/HCV Assay received FDA approval in February 2002 and CE (Conformité Européenne) Mark in Europe in January 2003 for use on the semi-automated PROCLEIX® System. The PROCLEIX® HIV-1/HCV Assay and System are commercially available in the United States and throughout Europe, Asia, Australia and New Zealand and are under evaluation in Latin America and several Asian countries.

The PROCLEIX® ULTRIO® Assay is a premium NAT product offering that adds the direct detection of hepatitis B virus (HBV) to the approved PROCLEIX® HIV-1/HCV Assay, allowing for three results to be obtained in the same amount of time using the same instrumentation. Over 350 million people worldwide are chronic carriers of HBV, with over 2 billion infected. HBV is the leading cause of liver

cancer in the world and is at its highest prevalence in Southeast Asia, Southern Europe, India and Africa. The PROCLEIX® ULTRIO® Assay received CE Mark Registration in Europe on the semi-automated PROCLEIX® System in January 2004 and on the fully automated, high-throughput PROCLEIX® TIGRIS® System in December 2004. We filed a Biologics License Application (BLA) in September 2004 in the United States for use of the PROCLEIX® ULTRIO® Assay on the PROCLEIX® System and the PROCLEIX® TIGRIS® System. On October 3, 2005, the FDA notified Gen-Probe that it considers the PROCLEIX® TIGRIS® System not substantially equivalent to the PROCLEIX® System for screening donated blood with the PROCLEIX® ULTRIO® Assay. Gen-Probe expects to file an amended BLA to respond to the FDA s questions contained in this complete review letter.

The PROCLEIX® WNV (West Nile Virus) Assay, a NAT product co-developed with Gen-Probe for the detection of WNV in plasma, whole blood, organs and tissue has been available for sale in the United States, under an Investigational New Drug, or IND, protocol and labeled For Investigational Use Only since June 2003. In December 2005, we received marketing approval for the PROCLEIX® WNV Assay on the semi-automated PROCLEIX® System. Since testing began under the IND application through December 2005, the PROCLEIX® WNV Assay has detected more than 1,500 West Nile virus contaminated units of donated blood, potentially preventing over 4,500 transfusion transmissions of the virus. The current market for this product is North America (the United States & Canada), although European and Latin American medical authorities have expressed interest in conducting epidemiological studies.

In addition to assays, we also sell equipment under the Gen-Probe collaboration. Blood Testing equipment includes:

- PROCLEIX® System;
- PROCLEIX® TIGRIS® System; and
- PROCLEIX® OPTIVA System

The PROCLEIX® System is a semi-automated instrument platform that is manufactured by Gen-Probe and marketed by Chiron and which has been commercially available since receiving FDA clearance in February 2002. The PROCLEIX® OPTIVA System, is a set of modular components that automate several of the steps performed manually with the PROCLEIX® System. A portion of the PROCLEIX® OPTIVA System, the Front-End Pipetor (FEP), received European CE Marking in June 2004. Another component, the PROCLEIX® OPTIVA Reagent Addition Station (RAS), received CE Marking in April 2005. The PROCLEIX® TIGRIS® System, a next generation, fully automated, high-throughput instrument platform, was launched in Europe in December 2004. It is also available under IND for use with the PROCLEIX® WNV Assay in the United States. The PROCLEIX® TIGRIS® System is manufactured for Gen-Probe and marketed by Chiron. By increasing throughput and automation, the PROCLEIX® TIGRIS® System is designed to allow smaller pool sizes and to enable individual donor testing (IDT) on a large scale, which is important for the detection of diseases with low viremic levels such as West Nile Virus and hepatitis B.

Through its joint business contractual arrangement with us, Ortho-Clinical Diagnostics sells a full line of immunodiagnostic tests for hepatitis viruses and retroviruses and provides supplemental tests and microplate and chemiluminescent instrument systems to automate test performance and data collection. We manufacture, and perform research on, viral antigens used by Ortho-Clinical Diagnostics to manufacture immunodiagnostic testing assays and supplemental hepatitis and HIV tests. Ortho-Clinical Diagnostics manufactures and sells the assays and instrument systems. Commercial products sold under the joint business contractual arrangement include RIBA® tests, which are immunodiagnostic

supplemental confirmatory tests for HIV and HCV developed and manufactured by us, and a line of immunodiagnostics screening tests for infectious diseases. We share equally in the pretax operating earnings generated under the contractual arrangement. The joint business contractual arrangement holds the immunodiagnostic rights to our hepatitis and retrovirus patents and receives royalties from hepatitis C virus and HIV tests sold by Abbott Laboratories, Inc. and from hepatitis C virus tests sold by Bio-Rad Laboratories, Inc. and certain other licensees.

Sales of nucleic acid testing products accounted for 14%, 14% and 11% of our consolidated total revenues in 2005, 2004 and 2003, respectively. Revenues related to our arrangement with Ortho-Clinical Diagnostics, including the joint business contractual arrangement, accounted for approximately 9%, 9% and 8% of our consolidated total revenues in 2005, 2004 and 2003, respectively.

Vaccines

Our vaccines segment offers approximately 20 influenza, meningococcal, travel, and pediatric and other vaccines. In our influenza franchise, our established brands include FLUVIRIN® vaccine, AGRIPPAL® vaccine, BEGRIVAC vaccine, and FLUAD® vaccine. Influenza, a contagious disease caused by the influenza virus, affects the respiratory tract, and can cause mild to severe illness, and sometimes death. Each year in the United States, on average 5% to 20% of the population get influenza, more than 200,000 people are hospitalized from influenza complications, and about 36,000 people die.

In July 2003, we acquired United Kingdom based PowderJect and commenced sales of FLUVIRIN® vaccine, a trivalent influenza vaccine. The vast majority of FLUVIRIN® vaccine production has been supplied to the U.S. market.

We manufacture AGRIPPAL® S1 and BEGRIVAC trivalent influenza vaccines and FLUAD® MF59 adjuvanted influenza vaccine in our Italian and German facilities and market them outside of the United States, largely in Europe. In 2005, we also distributed ENZIRA® influenza virus vaccine in the United Kingdom. ENZIRA® vaccine is manufactured by CSL Ltd. In July 2005, Chiron reported that it would be unable to supply any BEGRIVAC vaccine doses for the 2005-2006 influenza season due to a product sterility issue and wrote off its existing product inventory. Investigation of the product sterility issue has been completed and implementation of remedial measures and facility modifications is underway. In addition to our approved influenza virus vaccines, subsequent to December 31, 2005, we began to manufacture H5N1-strain candidate influenza virus vaccines under contract for various government pandemic stockpile programs.

In our meningococcal franchise, we sell MENJUGATE® vaccine, a conjugate vaccine against meningococcal disease caused by the bacterium *N. meningitidis* serogroup C, and MENZB , a meningococcal B vaccine developed to protect against a specific meningococcus B strain responsible for a 13-year epidemic in New Zealand. Invasive infection with the bacteria *N. meningitidis* can lead to meningococcal meningitis and septicemia (blood poisoning). Meningococcal meningitis can be caused by multiple serogroups (A, B, C, W, Y and others) and is associated with both mortality and morbidity. We have sold MENJUGATE® vaccine under a tender system to national governments and health systems in a variety of countries including various European countries, Canada, Argentina and Australia. We have sold MENZB in New Zealand.

Our travel vaccines franchise includes RABAVERT® and RABIPUR® rabies vaccines and ENCEPUR , a preservative-free tick-borne encephalitis vaccine.

Our pediatric and other vaccines include DTP, a diphtheria, tetanus and pertussis (whooping cough) vaccine; oral polio vaccine; and Vaxem Hib, glycoconjugate *Haemophilus Influenzae* vaccine. In 2000, we entered into agreements with Sanofi-Aventis (previously Aventis Pasteur MSD) for the distribution of FLUAD® vaccine and MENJUGATE® vaccine. Under the agreements, we market FLUAD® vaccine alone and we co-promote MENJUGATE® vaccine with Sanofi-Aventis in the United Kingdom and

Ireland. In the rest of Europe, Sanofi-Aventis distributes, co-markets and sells FLUAD® vaccine and MENJUGATE® vaccine under its own labels, ADIUGRIP and MENINVACT respectively. Our primary manufacturing facilities for vaccines are located in: Siena, Italy; Marburg, Germany; Liverpool, UK; and Ankleshwar, India. We mainly operate in India through a joint venture, Chiron Behring Vaccines Private Limited.

The principal markets for our manufactured vaccines and vaccines that we market under license are the United States, Germany, Italy, and the United Kingdom. We have two vaccines licensed in the United States: FLUVIRIN® influenza virus vaccine and RABAVERT® rabies vaccine. We also supply diphtheria and tetanus (DT) concentrate to GlaxoSmithKline for use in its DT-containing vaccines licensed by the FDA.

In addition, we market our vaccines in other European countries and in the Middle East, the Far East, Africa and South America, and to international health agencies such as UNICEF and the Pan American Health Organization.

In addition to revenues from the sale of the vaccines described above, we receive royalties from the sale of certain vaccines by Merck and Company, Inc. and GlaxoSmithKline, based upon technology developed by us. Merck s hepatitis B virus vaccine, based on Chiron technology, was the first genetically engineered vaccine licensed by the FDA for human use.

Sales of our influenza vaccine franchise products accounted for approximately 12%, 9%, and 19% of our consolidated total revenues in 2005, 2004 and 2003, respectively. In 2005, 2004, and 2003, sales of FLUVIRIN® vaccine accounted for 5%, 0%, and 12% of our consolidated total revenues. As a result of the MHRA s suspension of our license to manufacture FLUVIRIN® vaccine from October 5, 2004 through March 2, 2005, we had no sales of FLUVIRIN® vaccine in 2004 other than $2.3 million in late 2003-2004 season sales. Sales of pediatric and other vaccines accounted for approximately 9%, 12% and 11% of our consolidated revenues in 2005, 2004 and 2003, respectively. No other single vaccine product or class of vaccine product accounted for 10% or more of our consolidated total revenues in any of the last three fiscal years.

On March 16, 2006, we announced a recall and withdrawal of MORUPAR®, our measles, mumps and rubella (MMR) vaccine. We previously supplied MORUPAR® vaccine to customers in a limited number of developing countries, largely via the United Nations Children s Fund (UNICEF) and the Pan American Health Organization (PAHO), and to Italy. Results of pharmacovigilance surveillance in Italy suggest that MORUPAR® vaccine may be associated with a higher reported rate of adverse events following immunization than other MMR vaccine products. We expect to work with the World Health Organization (WHO) to assist it in conducting a risk-benefit analysis to determine whether UNICEF or PAHO will require a limited quantity of the existing inventory of MORUPAR® vaccine for their ongoing public health programs. We have written-off in 2005 approximately $6.0 million of MORUPAR® inventory as a result of the withdrawal and recorded approximately $1.7 million of product returns reserves in 2005 in connection with expected returns of 2005 product sales from the recall.

Biopharmaceuticals

Our biopharmaceutical segment discovers, develops, manufactures and markets a range of therapeutic products primarily for cancer and infectious and pulmonary disease. The following describes our primary marketed products.

TOBI® tobramycin solution for inhalation, USP *We* manufacture and market TOBI® solution, a stable, premixed, proprietary formulation of the antibiotic tobramycin for delivery by inhalation using a nebulizer. TOBI® solution has been tested and approved for cystic fibrosis patients with *Pseudomonas aeruginosa* lung infections and is the first and only inhaled antibiotic solution to be approved by the FDA

for cystic fibrosis. Cystic fibrosis is caused by a genetic mutation that prevents cells from building a special protein required for normal movement of sodium chloride (salt) in and out of cells lining the lungs and other organs. This abnormal movement causes secretion of thick, sticky mucus in the airways. This mucus is not cleared from the airways and, as a result, bacteria begin to grow, causing infection. *Pseudomonas aeruginosa* is the most common bacterium causing lung infections in people with cystic fibrosis. In cystic fibrosis patients with pseudomonal lung infections, tobramycin is the most commonly used intravenous antibiotic. The advantage of inhalation is that it permits higher antibiotic concentrations in the lung and reduces side effects by limiting systemic exposure. Treatment with TOBI® solution decreases the bacterial load and improves overall lung function. We market the TOBI® solution in the United States, the European Union, Canada, Switzerland, Norway, Israel, Argentina and Brazil.

PROLEUKIN® (aldesleukin) for injection *We* manufacture and market PROLEUKIN® (aldesleukin), a recombinant form of interleukin-2. Interleukin-2 is a protein produced naturally in the body in very small quantities, which stimulates the immune system to increase the production and function of immune cells.

While the precise anti-tumor mechanism of PROLEUKIN® (aldesleukin) is unknown, research has demonstrated that PROLEUKIN® (aldesleukin) induces the proliferation of immune cells, including natural killer and cytotoxic T cells that can recognize and mobilize against tumor-specific antigens on the surface of malignant cells. We market PROLEUKIN® (aldesleukin) directly or through distributors in the United States and over 50 other countries in North America, Europe, Asia and South America to treat metastatic renal cell carcinoma (a type of kidney cancer), and in the United States and Canada to treat metastatic melanoma (a form of skin cancer). Studies have demonstrated that PROLEUKIN® (aldesleukin) offers the possibility of a complete and long-lasting remission in these diseases.

BETASERON® (interferon beta-1b) for SC injection *We* manufacture BETASERON® (BETAFERON® in Europe) interferon beta-1b which is marketed by Schering AG and its affiliates, including Berlex Laboratories, Inc. (collectively, Schering). Boehringer Ingelheim also supplies BETAFERON® interferon beta-1b to Schering for sale in Europe. Multiple sclerosis is an autoimmune disease in which the patient s immune system attacks and destroys an element of the patient s own central nervous system. The active ingredient in BETASERON® is a modified form of a beta interferon produced naturally by the human body. Interferons help to regulate the immune system, and BETASERON® interferon beta-1b is thought to help slow down the immune system s attack on nerve tissue. While the ways in which BETASERON® interferon beta-1b actually affects multiple sclerosis are not clearly understood, it has been demonstrated clinically that BETASERON® interferon beta-1b may decrease the nerve damage associated with multiple sclerosis. It has been shown to reduce the overall frequency of multiple sclerosis relapses, which are also called exacerbations or attacks, as well as the number of moderate and severe relapses. BETASERON® interferon beta-1b is approved for relapsing/remitting multiple sclerosis in over 70 countries, including the United States and the nations of the European Union, and for secondary progressive multiple sclerosis in approximately 60 countries, including the nations of the European Union, Canada, Australia and New Zealand. In 2002, we and Schering AG launched a room temperature formulation of BETASERON® interferon beta-1b, which is the only beta interferon currently marketed in the United States that can be stored at room temperature long term up to two years. To further increase ease of use, Chiron and Schering AG introduced a diluent syringe presentation for BETASERON® interferon beta-1b in the United States in January 2004 and in Japan in December 2003. On February 24, 2006 Schering AG notified Chiron of its intention to exercise its option under the companies Regulatory Filing, Development and Supply Agreement to purchase or lease all assets used by Chiron in the manufacture for Schering of BETASERON® interferon beta-1b products and all contractual rights at their fair market or lease value. The purchase/lease option is subject to the closing of the

proposed acquisition of Chiron by Novartis AG. The agreement requires that the value be determined by an independent third party mutually agreed upon by both parties.

CUBICIN® (daptomycin) *In* January 2006, European Commission granted marketing approval to Chiron for CUBICIN®, a first-in-class IV antibiotic. The marketing approval was granted in the 25 member states of the European Union, Iceland, Liechtenstein and Norway. Under the approval, CUBICIN® is indicated for the treatment of complicated skin and soft-tissue infections (cSSTI) caused by Gram-positive bacteria. The CUBICIN® antibiotic is also approved by the FDA for the treatment of complicated skin and skin structure infections caused by Gram-positive bacteria, and is marketed in the United States by Cubist Pharmaceuticals, Inc. We acquired marketing rights to the antibiotic for certain countries outside of the United States from Cubist. CUBICIN® antibiotic is manufactured for us by Cubist Pharmaceuticals, Inc.

CARDIOXANE dexrazoxane (ICRF-187) *Dexrazoxane* is the only cardioprotectant indicated to prevent cardiac damage induced by anthracyclines, a group of chemotherapy medications used to treat a variety of cancers. CARDIOXANE dexrazoxane is currently approved in 31 countries in over four continents.

Our biopharmaceutical products are manufactured primarily in our Emeryville, California and Vacaville, California facilities. Sales of TOBI® formulation accounted for approximately 12%, 12% and 10% of our consolidated total revenues in 2005, 2004 and 2003, respectively. Revenues from BETASERON® interferon beta-1b, which include product sales to Schering and royalties earned on Schering s European sales of BETAFERON® interferon beta-1b, accounted for approximately 11% (7% product sales and 3% royalties), 11% (8% product sales and 3% royalties) and 11% (7% product sales and 4% royalties) of our consolidated total revenues in 2005, 2004 and 2003, respectively. No other biopharmaceutical product accounted for 10% or more of our consolidated total revenues in any of the last three fiscal years.

Research and Development

Our research and development focuses on the prevention and treatment of cancer and infectious and pulmonary diseases. In addition to our research and development activities, technologies that are developed in collaborations with third parties, as well as technologies licensed from outside parties, also are sources of potential products for our segments. Products or product candidates that are inappropriate for our commercial organization are often out-licensed to other companies.

Blood Testing

Chiron pursues research and development of assays for transfusion-transmitted diseases, such as variant Creutzfeldt-Jakob disease (vCJD). In August 2004, we supplemented our existing vCJD research and development program by acquiring Prion Solutions, Inc., a privately held company focused on research into vCJD and other prion-related diseases.

We also participate in the development of a range of hepatitis and retrovirus immunoassays for use in screening of donated blood, plasma, organs and tissue and in-vitro clinical diagnostics through our joint business contractual arrangement with Ortho-Clinical Diagnostics.

We moved beyond Blood Testing and into the broader realm of blood safety when we entered into a collaboration with ZymeQuest in 2003 to develop and commercialize ZymeQuest s enzyme conversion system. This system is designed to convert groups A, B and AB red blood cells to enzyme-converted universal blood group O (ECO). This technology could fill a critical need for blood and transfusion centers since between 5% and 10% of the global donated blood supply is discarded each year due to non-matches between donated blood and patients blood type requirements. We made an equity investment in

ZymeQuest and obtained worldwide marketing and commercial rights to the technology. In 2005 we initiated the pre-pivotal clinical trial for the conversion of type A red blood cells to ECO, or A-ECO.

Vaccines

Our vaccines segment research and development is focused on developing next generation influenza manufacturing capability, developing new vaccines for pandemic preparedness and broadening our meningococcal franchise. Next generation cell culture production technology may offer significant advantages over traditional methods of influenza vaccine manufacturing by eliminating the dependence on chicken eggs for production. The removal of egg supply lead times may enable a more flexible start-up of vaccine production in the event of an annual vaccine supply shortfall or an avian influenza pandemic. In Europe, we completed an initial Phase 3 study of our influenza cell culture vaccine in the 2004-2005 influenza season, in which the vaccine demonstrated satisfactory safety and immunogenicity, and we are conducting the remainder of the Phase 3 program during the 2005-2006 influenza season. In the United States we are conducting Phase 1 / Phase 2 studies during the 2005-2006 influenza season.

World health agencies are concerned about recent outbreaks of highly pathogenic avian influenza in poultry and a limited number of humans and are concerned that the present situation could give rise to another influenza pandemic. In 2004, we were awarded contracts by the National Institutes of Health (NIH) for production of H5N1 and H9N2 candidate vaccines, to be used by the National Institute of Allergy and Infectious Diseases (NIAID) in clinical studies of safety and immunogenicity. The H9N2 candidate vaccine study was completed, using H9N2 antigens with and without Chiron s adjuvant MF59, and preliminary data indicated that the vaccine formulations containing the adjuvant MF59 proved highly immunogenic, inducing antibody levels believed to confer protection against the influenza strain while the unadjuvanted vaccine induced significantly lower antibody titers. The NIAID study using our H5N1 candidate vaccine is ongoing. We have entered into supply contracts with several governments, including the U.S. and the UK governments, for influenza vaccines for stockpiles based on the H5N1 avian influenza strain. The commercial potential for stockpiling is unclear due to among other things, the fact that larger demands would require greater capacity, the fact that production for stockpiling can only occur between normal seasonal campaigns, and government pressure on pricing. There are also technical obstacles that need to be addressed in order to produce a commercial pandemic vaccine.

In our meningococcal franchise, we are expanding our product line beyond MENJUGATE® vaccine, our conjugate vaccine against Meningococcus C infection, through the development of other vaccines against additional Meningococcal strains responsible for human disease. Meningococcal disease is associated with infections affecting the membranes around the brain and spinal cord or the bloodstream, and can result in brain damage, blindness, deafness, limb amputations and death. Infection may be fatal even if diagnosed early, making prevention essential. Young children and persons in close living quarters such as college dorms or military facilities are at highest risk for meningococcal disease.

Serotype B, along with serotypes A, C, W and Y cause approximately 95% of the meningococcal infections worldwide. Multivalent vaccines are effective against more than one serotype. We are developing a tetravalent conjugated vaccine against serotypes A, C, W and Y and we are completing Phase 2 studies of this ACWY vaccine in a variety of age groups, including ages under two.

In 2004, we began distributing a meningococcal B vaccine in New Zealand, MENZB , to protect against the specific meningococcal B strain responsible for a 13-year epidemic in that country. While our current meningococcal B product, MENZB is efficacious against only a single strain of meningococcal B, we are also developing a second-generation vaccine candidate utilizing our novel genomic approach against Meningococcus B, a disease for which no broadly efficacious vaccine is currently available. Our meningococcal B vaccine was in a Phase 1 clinical trial in 2005.

Through collaborations, we are obtaining human safety and immunogenicity information on hepatitis C virus vaccine candidates, and our vaccine against HIV, which is in Phase 1 testing in collaboration with NIH. We are also developing novel adjuvants, compounds that amplify the immune response generated by vaccine antigens.

Biopharmaceuticals

Research and development in the biopharmaceutical segment focuses on protein and small molecule therapies for cancer and infectious and pulmonary disease.

Infectious and Pulmonary Disease

Tifacogin (recombinant Tissue Factor Pathway Inhibitor) *Tifacogin* a coagulation inhibitor, was developed in collaboration with Pfizer, Inc. In October 2003 we acquired all of Pfizer, Inc. s interest in tifacogin, in return for which Pfizer will receive royalties on sales of tifacogin. In 2004 we initiated CAPTIVATE, a Phase 3 trial for tifacogin in patients with severe community-acquired pneumonia (CAP). CAP is a serious infection of the lungs caused by various, well-defined pathogens. Severe CAP affects approximately 300,000 patients in the United States annually requiring ICU admission, of whom approximately 30 percent die. In December 2005 an independent Data Monitoring Committee completed an interim analysis of clinical data from the study and recommended the continuation of the study.

Tobramycin inhalation powder (TIP) *In* December 2001, we entered into a collaboration with Nektar Therapeutics Inc. (Nektar) to develop and register an inhalable dry-powder formulation of the antibiotic tobramycin as an extension of our TOBI® formulation franchise. TIP is used with Nektar s new hand-held, fully portable device. We are currently conducting Phase 3 clinical trials of the product.

Oncology

Using a translational-medicine approach to drug development, Chiron s research department continues to feed a growing oncology pipeline, which includes CHIR-258, CHIR-12.12 and CHIR-265.

CHIR-258 (growth factor kinase inhibitor) *CHIR-258* is a novel, orally available, highly selective, multi-targeted receptor tyrosine kinase inhibitor, which acts on both tumor cell growth and angiogenesis. As of January 2006, disease-specific Phase 1 studies of CHIR-258 are ongoing in acute myelogenous leukemia (AML), multiple myeloma and melanoma.

CHIR-12.12 *CHIR-12.12 is a novel, highly potent, fully human antagonist monoclonal antibody that targets the CD40 antigen*. In 2005, we initiated two Phase 1 studies of CHIR-12.12 - one in patients with chronic lymphocytic leukemia and a second in patients with multiple myeloma, both types of cancer that are associated with expression of the CD40 antigen on the cancer cell surface. This is the first project being developed under our collaboration agreement with XOMA Ltd. for the commercialization of therapeutic antibodies for cancer.

CHIR-265 In December 2005 we filed an IND for CHIR-265, a novel, orally available, highly selective Raf kinase inhibitor.

Research and Development Expenses and Related Revenues

Research and development expenses for the years ended December 31, 2005, 2004 and 2003 for Chiron-sponsored research, including payments to collaboration partners, were $433.9 million, $431.1 million and $409.8 million, respectively. Under contracts where we recognize revenue based upon research and development work performed, the revenues amounted to $16.3 million, $20.9 million and $16.8 million in 2005, 2004 and 2003, respectively. We recorded these revenues in Collaborative agreement revenues and Other revenues in the Consolidated Statements of Operations. Generally,

these revenues include fees for research services as they are performed or completed and milestone payments upon attainment of specified benchmarks.

Business Relationships

We have important business relationships with various companies, including the following.

Gen-Probe Incorporated

We have a collaboration with Gen-Probe relating to the development and commercialization of NAT products under the PROCLEIX® brand name to screen donated blood, plasma, organs and tissue for viral infection. PROCLEIX® assays and systems incorporate NAT technology to detect viral RNA and DNA in donated blood and plasma during the very early stages of infection, when those infectious agents are present but cannot be detected by immunodiagnostic tests. Gen-Probe manufactures the NAT assays and certain instruments, and Chiron sells both assays and instruments under the PROCLEIX® brand name. Effective January 1, 2004, under an amendment to the worldwide blood screening collaboration agreement with Gen-Probe, permanent, fixed revenue sharing percentages were adopted for each party. Gen-Probe s share was set at 45.75% of net revenues for assays that include a test for the hepatitis C virus. For commercial assays, that do not test for hepatitis C virus, such as the West Nile Virus assay, each party receives 50% of the net revenues after deduction of specified expenses.

Ortho-Clinical Diagnostics, Inc.

We have a joint business contractual arrangement with Ortho-Clinical Diagnostics relating to the development and commercialization of immunodiagnostic tests using recombinant DNA and antibody technologies to detect retroviruses and hepatitis viruses in blood. Under the terms of the arrangement, Ortho-Clinical Diagnostics manufactures and sells the assays and instrument systems, and Chiron supplies raw materials for the assays. Chiron and Ortho-Clinical Diagnostics share equally in the pretax operating earnings generated by the joint business contractual arrangement. Our joint business arrangement with Ortho-Clinical Diagnostics is operated under a contractual arrangement and is not a separate and distinct legal entity. The joint business contractual arrangement holds the immunodiagnostic rights to our hepatitis and retrovirus patents and receives royalties from the sale of hepatitis C virus and HIV tests sold by Abbott Laboratories, Inc. and from sales of hepatitis C virus tests by Bio-Rad Laboratories, Inc. and certain other licensees.

Cubist Pharmaceuticals

In October 2003, we entered into a license agreement for the development and commercialization of Cubist s antibiotic, CUBICIN® daptomycin, in Western and Eastern Europe, Australia, New Zealand, India and certain Central American, South American and Middle Eastern countries. Under the agreement, we are obligated to pay upfront payments, regulatory and sales milestones, and a tiered royalty on CUBICIN® daptomycin sales in the territories.

Schering AG and Berlex Laboratories, Inc.

Chiron and Berlex, Inc., a subsidiary of Schering AG of Germany, jointly developed BETASERON® (BETAFERON® in Europe) interferon beta-1b. Under the terms of the Regulatory Filing, Development and Supply Agreement with Schering AG, BETASERON® product is manufactured by us and sold in the United States and Canada by Berlex. BETAFERON® interferon beta-1b is manufactured by us and Boehringer Ingelheim and is sold by Schering AG in Europe. BETAFERON® and BETASERON® revenues recognized under this agreement contributed 11% of our consolidated total revenues in each of 2005, 2004 and 2003. Under the agreement, for product manufactured by us and marketed by Schering AG

and its affiliates, including Berlex, we receive revenue, which is recorded as product sales. For product manufactured by Boehringer Ingelheim and marketed by Schering in Europe under the trade name BETAFERON®, we receive royalties net of Schering s supply costs. The Regulatory Filing, Development and Supply Agreement expires in October 2008 unless renewed. On February 24, 2006 Schering AG notified Chiron of its intention to exercise its option under the Regulatory Filing, Development and Supply Agreement to purchase or lease all assets used by Chiron in the manufacture for Schering of BETASERON® interferon beta-1b products and all contractual rights at their fair market or lease value. The purchase/lease option is subject to the closing of the proposed acquisition of Chiron by Novartis AG. The agreement requires that the value be determined by an independent third party mutually agreed upon by both parties.

Nektar Therapeutics, Inc.

In December 2001, we entered into a collaboration with Nektar (then operating as Inhale Therapeutic Systems) to develop and register an inhalable dry-powder formulation of the antibiotic tobramycin as an extension of our TOBI® formulations franchise. Under the terms of the collaboration, Nektar is responsible for development of the dry powder formulation and inhalation device, as well as supplying drug product for clinical trials and the market. Chiron is responsible for all other aspects of drug development including clinical trial conduct, regulatory submissions, preparation for product launch and sales and marketing of the final drug product. Under the agreement, we are obligated to pay upfront payments and development milestones, and we will pay royalties when the product is commercialized.

XOMA Ltd.

We have a worldwide, exclusive, multi-product, collaborative agreement with XOMA for the development and commercialization of antibody products for the treatment of cancer. Under the terms of the agreement, we and XOMA agreed to jointly research, develop, and commercialize multiple antibody product candidates. Under the agreement, we also share development and commercialization expenses, including preclinical and clinical development, manufacturing and worldwide marketing costs, as well as revenues, generally on a 70-30 basis, with Chiron s share being 70% and XOMA s share being 30%. We made an initial payment of $10.0 million, and have made a loan facility of up to $50.0 million available to XOMA, starting on January 1, 2005 to fund 75% of XOMA s share of development expenses. Under this arrangement, we made $12.1 million in loan advances to XOMA as of December 31, 2005.

Commercialization

Technologies arising out of our research and development efforts are commercialized in various ways:

- We market and distribute certain products, either directly or through distributors. See Sales and Marketing below.

- We develop other products in collaboration with third parties. Under collaboration agreements, marketing rights may be assigned to us or to the collaborator or shared by both parties. In the event rights are assigned to us, we generally pay royalties to or enter into revenue split agreements with our collaborator. In the event marketing rights are assigned to the collaborator, we often retain the right to manufacture and supply key raw materials.

- We license other technologies to third parties, with the licensee assuming responsibility for further development. We generally receive royalties on sales of the resulting product. Selected agreements under which we currently derive royalty revenues for technologies licensed to third parties include:

- Licenses to F. Hoffmann-La Roche Ltd. and Roche Molecular Systems, Inc. under our hepatitis C virus and HIV related patents for use in nucleic acid amplification in *in vitro* diagnostics and in blood screening.

- An agreement with Schering AG relating to BETASERON® (BETAFERON® in Europe) interferon beta-1b as described above.

- An agreement with Bayer Corporation relating to, among other things, use of our hepatitis C virus and HIV technologies for nucleic acid amplification in *in vitro* diagnostics.

- A license agreement with Laboratory Corporation of America Holdings (LabCorp) and its affiliates, for our HCV intellectual property for nucleic acid testing (NAT).

- A non-exclusive license agreement with the Blood Transfusion Centers of the German Red Cross (Blutspendediensten des Deutsche Rotes Kreuz, or DRK), for the use of our HCV technology for use in molecular probe homebrew blood screening.

Sales and Marketing

Blood Testing

Global marketing and distribution and our U.S. sales organization for nucleic acid testing products are based in Emeryville, California. Blood Testing has representatives around the world. International sales are conducted out of regional offices, including our primary offices located in Paris, France and Hong Kong, China. We sell products to the public sector through tenders (a bid solicitation process) and to private sector blood banks directly and through distributors.

In 2002, we signed a multi-year agreement with the American Red Cross, which collects approximately 50% of the 14 to 15 million units of blood collected in the United States each year. Under that agreement, the American Red Cross purchases from Chiron certain products, instrumentation and services that enable the American Red Cross to perform amplified nucleic acid screening on the blood it collects. Currently we are a party to multi-year contracts awarded through the tender process with the public sector blood services of many countries outside the United States, with the most significant in terms of donations being Australia, Italy, South Africa and the United Kingdom.

Vaccines

Our vaccines marketing and sales organization is based in Marburg, Germany for the German market, in Siena, Italy for the Italian market, and in Oxford, United Kingdom for the United Kingdom market. In 2004, we established a U.S. Vaccines headquarters in Philadelphia, Pennsylvania. In general, we market our influenza and rabies vaccines in the United States through a network of wholesalers and distributors. In the United States our direct sales efforts are focused on public health, distributor channels, and non-traditional channels, e.g., employers, chain drug headquarters and service providers. Internationally, our direct sales efforts are focused on pediatricians and general practitioners. We also sell products to the public sector through tenders and to private sector pharmacies directly and through wholesalers and distributors.

BioPharmaceuticals

Our biopharmaceutical marketing and sales organization for the United States is headquartered in Emeryville, California, and European operations are headquartered in Uxbridge, United Kingdom. We focus our sales efforts on specialist physicians, principally oncologists, urologists and pulmonologists, who are based in hospitals and large clinics. Generally, we sell products to wholesalers, distributors, clinics and hospital pharmacies.

Competition

We operate in a highly competitive environment, and we expect competition to increase. Competitors include large pharmaceutical and blood testing companies, and biotechnology companies. Some of these competitors, particularly large pharmaceutical and blood testing companies, have greater resources than we have. We and our competitors apply rapidly evolving technologies and new developments that frequently result in price competition and product obsolescence. Substantial consolidation is underway in the global healthcare industry and is expected to produce greater efficiencies and even more intense competition. To compete effectively, we invest heavily in research and development, maintain specialized sales forces that concentrate on individual classes of customers and spend significant amounts on marketing, promotion and selling.

Important biotechnology research is performed in universities and nonprofit research organizations. These entities are becoming more active in seeking patent protection and licensing revenues for their discoveries. The competition among large pharmaceutical companies and smaller biotechnology companies to acquire technologies from these entities also is intensifying. We actively collaborate with such entities in research, and have and will continue to license their technologies for further development. However, these institutions also compete with us to recruit scientific personnel and to establish proprietary positions in technology.

Blood Testing

The PROCLEIX® product line is based on proprietary Transcription Mediated Amplification (TMA) technology developed by Gen-Probe. The primary competition is with polymerase chain reaction (PCR) based products. PCR-based products are supplied to the market by F. Hoffmann-La Roche, a Chiron licensee, or developed in-house by blood banks (referred to as homebrew). The commercial market for nucleic acid testing products in the blood banking and plasma industries has developed rapidly as regulatory agencies in developed countries began in 1999 to introduce policies and mandates that require this new technology to be implemented as an additional measure to improve blood safety. In developing countries there has been a move to implement nucleic acid based tests in the private health care sector and we anticipate this expanding to the public arena over the next several years. Competition in this sector is the same as in the developed countries.

We are the sole manufacturer of hepatitis C virus antigens for use in immunodiagnostic assays sold by the joint business contractual arrangement with Ortho-Clinical Diagnostics. We also manufacture hepatitis C virus antigens for Abbott Laboratories, Inc. s immunodiagnostic assays. In the immunodiagnostic blood testing market, the Ortho-Clinical Diagnostics joint business contractual arrangement competes with Abbott Laboratories. The joint business contractual arrangement has experienced increased competitive pressures from Abbott Laboratories ABBOTT PRISM® instrument system. The joint business contractual arrangement also develops and sells immunodiagnostic instruments and assays to detect hepatitis, retrovirus and other agents in clinical diagnostic applications. Many other companies, including F. Hoffmann-LaRoche Limited and Bayer Corporation, are significant competitors with respect to these products.

Vaccines

Four large companies hold the majority share of the worldwide vaccines business: Merck, GlaxoSmithKline, Wyeth and Sanofi-Aventis. We are the world s fifth largest vaccines company. Sanofi-Aventis has a strategic alliance with Merck in Europe. All of these companies have substantial research and development programs. Additionally, there is a number of biotechnology companies involved in research programs, primarily involving a limited range of vaccines. We are aware of a variety of companies that are developing influenza vaccine cell culture manufacturing technology.

The competitive factors in vaccines are proven ability to supply product, price, the introduction of new products including vaccines against diseases for which no vaccine was previously available and new combination vaccines which can prevent several diseases in a single product. Public health authorities, medical practitioners and patients frequently favor combination vaccines, particularly in pediatric vaccines, because they eliminate the need for multiple injections and may increase overall compliance with recommended vaccination schedules. As new combination vaccines are introduced, older combinations and single products often become obsolete. We may be limited in our ability to develop and market certain combination vaccines if one of the vaccines, which would otherwise be included in the combination, is covered by valid and enforceable patents or other proprietary rights held by third parties.

Prior to the suspension of our Liverpool manufacturing license from October 5, 2004 through March 2, 2005, we were one of two primary suppliers of influenza vaccine to the United States. Although the license suspension has been lifted, our inability to supply FLUVIRIN® vaccine during the 2004-2005 influenza season has led a competitor to introduce an influenza vaccine product in the United States during the 2005-2006 season and we expect competition to continue to increase. Our influenza vaccines approved in Europe also remain competitive there. Competition varies by region according to product license approvals. All influenza vaccines producers, including us, face an annual change in influenza strains, which can act as a barrier for new competitors.

MENJUGATE®, our meningococcal C vaccine, faces competition from vaccines produced by two other companies, Baxter International, Inc. and Sanofi-Aventis. These companies are also competing for future meningococcal vaccine business worldwide.

Biopharmaceuticals

TOBI® tobramycin solution for inhalation is the first and only inhaled antibiotic solution to be approved by the FDA for the treatment of infection associated with cystic fibrosis. The use of oral and intravenous antibiotics to treat pseudomonal and other bacterial infections is well established and in cystic fibrosis patients with pseudomonal lung infections, tobramycin is the most commonly used intravenous antibiotic. The advantage of inhalation is that it permits higher antibiotic concentrations in the lung and reduces side effects by limiting systemic exposure. Competitive medical therapies include generic antibiotics, anti-inflammatory drugs, pharmacist compounded tobramycin solutions, oral replacement enzymes to maintain nutrition and mucolytics to clear pulmonary secretions. In 2005, Chiesi, a competitor, obtained MRP positive opinion and local approval in Italy for their cystic fibrosis product.

PROLEUKIN® (aldesleukin) for injection is one of two products approved by the FDA to treat metastatic renal cell carcinoma and also one of two approved treatments for metastatic melanoma. In addition to longstanding competition for products, such as alpha interferons sold by Schering-Plough Corporation, recent years have been marked by heightened clinical trial activity that has expanded treatment options for patients, particularly in the area of kidney cancer. Enrollment in these trials and related off-label use has reduced the new patient population available for PROLEUKIN® (aldesleukin) in 2005. In December 2005, an orally available kinase inhibitor, Nexavar, jointly sold by Bayer HealthCare and Onyx Pharmaceuticals, was the first of these products previously available in clinical trials to obtain marketing approval from the FDA to treat kidney cancer patients. This was followed by FDA approval, in January 2006, of Pfizer s Sutent (sunitinib), an anti-cancer treatment for patients advanced kidney cancer and with gastrointestinal stromal tumors (GIST), a rare stomach cancer. We expect competitive pressures from newly approved products and products currently in clinical trials to continue in the future.

BETASERON® (interferon beta-1b) for SC injection, as a treatment for multiple sclerosis, competes with AVONEX®, a recombinant beta interferon, sold by Biogen Idec, Inc., REBIF®, a recombinant beta interferon, from Serono, S.A. (Serono), marketed and sold in the United States by Pfizer Inc., and COPAXONE® glatiramer acetate injection from Teva Pharmaceutical Industries, Ltd. NOVANTRONE®

mitoxantrone for injection concentrate is marketed and sold by Serono for the treatment of secondary progressive multiple sclerosis. In addition, BETASERON® interferon beta-1b competed for a number of months with TYSABRI®, a humanized monoclonal antibody which was marketed by Biogen Idec, Inc. and Elan Pharmaceuticals until marketing was suspended by these companies in February 2005. The multiple sclerosis market is highly competitive, and will remain so as various other companies have treatments for multiple sclerosis in clinical development.

Government Regulation

Regulation by governmental authorities in the United States and other important locations is a significant factor in the manufacture, marketing and sale of our products and in our research and development activities.

For all of our products, the time and expense needed to complete the required clinical studies, prepare and submit the required applications and supporting documentation and respond to inquiries generated by regulatory review can far exceed the time and expense of the research initially required to create the product. These factors largely determine the speed with which a successful research program is translated into a marketed product.

Blood Testing

In the United States, Blood Testing products, whether based upon nucleic acid testing or immunodiagnostic testing technologies, may only be commercially sold pursuant to the terms of approval of specific license applications in which the product s safety and effectiveness must be demonstrated based upon well-controlled studies. Upon approval of the license application, the product may be marketed for the specific uses, which were identified in the approval. Facilities, processes and operations used for the manufacture, testing, storage and distribution of our Blood Testing products in the United States are subject to FDA approval and periodic inspection.

In Europe, our Blood Testing products are regulated through the In Vitro Diagnostic Medical Devices Directive. In other geographic areas, such as Australia, Canada and Mexico, local regulatory authorities regulate Blood Testing products.

Vaccines and Biopharmaceuticals

In the United States, our therapeutic and vaccine products (both commercial and investigational) are primarily regulated under federal law and are subject to rigorous FDA approval procedures. No product can be marketed in the United States until an appropriate application is approved by the FDA. The FDA applies the approval procedures on a product-by-product basis and typically requires, among other things, an extensive three-phase human clinical testing program. In Phase 1, studies are conducted with a relatively small number of subjects to assess the safety of the product. In Phase 2, the product is evaluated in a larger group of subjects to begin to assess efficacy and appropriate dosing. Phase 3 studies are conducted in the target population with a number of subjects that is large enough to provide sufficient data to establish statistically the safety and efficacy of the product. The FDA approves products to treat specified medical conditions or disorders. Further studies would be required to market the product for other uses. The FDA must inspect and approve all facilities used to manufacture, fill, test and distribute biologic products. If any change in manufacturing facilities or processes occurs after FDA approval, additional regulatory review and possibly additional clinical studies may be required. In addition to standard regulatory procedures, many governments have provisions for use of otherwise unapproved medical products in a public health emergency.

Licensing procedures in Europe are comparable to those in the United States. In 1995, the European Union established a centralized procedure for licensing of products derived from the use of high

technology/biotechnology processes. This procedure leads to the grant of a single license for the entire European Union. Effective January 1, 1998, the European Union has also adopted a decentralized procedure under which a license granted in one member state is mutually recognized by the other member states, leading to a grant of licenses in member states recognizing the original license. This procedure is replacing independent national licensing of products in the European Union. In addition, products must receive country-pricing approvals in some territories before they can be marketed in that country.

Patents and Intellectual Property Rights

Patents are very important to our business. We have a policy of seeking patents on inventions arising from our research and development activities. The time and expense required to develop and obtain regulatory approval to market human healthcare products is significant. Without the protection of patents or trade secrets, competitors may be able to use our inventions to manufacture and market competitive products without being required to undertake the lengthy and expensive development efforts made by us. We also receive significant revenue through the licensing of these patents to third parties. We have a substantial number of granted patents and pending patent applications in the United States and other important markets. Additionally, we have licensed a number of patents and patent applications from third parties. Additional information is provided below on the certain patents held or licensed by us that relate to our key products. The existence of such patents does not mean they are valid or can be enforced against competitive products. We seek term extensions for some patents, which are available in certain countries based on delays in the grant of regulatory approvals for the sale of products covered by these patents. For these reasons the expiration dates provided below are not definitive.

We consider our trademarks and registered trademarks and those of our subsidiaries, in the aggregate, to be of material importance. All are covered by registrations or pending applications for registration in the U.S. Patent and Trademark Office and in other countries. Trademark protection continues in some countries for as long as the mark is used and, in other countries, for as long as it is registered. Registrations generally are for fixed, but renewable price terms.

Trade secrets and confidential information are also important to our commercial success. Although we seek to protect trade secrets and confidential information, others may obtain access to such information or develop the same or similar information independently. Also, third parties may obtain patent protection that precludes us from using our trade secrets or confidential information.

This report also includes trademarks, service marks and trade names of other companies.

Blood Testing

The PROCLEIX® HIV-1/HCV Assay is covered by numerous patents held by us in the United States and worldwide. These patents contain claims directed to methods of hybridization and methods for determining the presence of the hepatitis C virus in a sample and to probes/primers utilized in such a process. The hepatitis C virus patent family for NAT expires in the United States in 2015 and ex-U.S. in 2010. The HIV patent family expires in the United States in 2020. The HIV patent family expired ex-U.S. in 2005. The PROCLEIX® System product line is also covered by several patents held by Gen-Probe and licensed to us for use in blood testing.

The PROCLEIX® ULTRIO® Assay is covered by several patents held by Gen-Probe and licensed to us for use in Blood Testing. The PROCLEIX® WNV Assay is covered by several patents and pending applications held by Gen-Probe and licensed to us for use in Blood Testing.

The hepatitis C virus immunoassay diagnostic products sold by our joint business contractual arrangement with Ortho-Clinical Diagnostics are covered by numerous patents in the United States and worldwide. These patents contain claims directed to hepatitis C virus immunoassay methods, kits and

hepatitis C virus polypeptides. In the United States, certain patents expire between 2011 and 2017. The corresponding European family of patents expires in 2010.

The HIV immunoassay diagnostic products sold by our joint business contractual arrangement with Ortho-Clinical Diagnostics are covered by numerous patents in the United States and worldwide. The earliest patents expire in 2009 in the United States and expired in 2005 in Europe.

We own additional HCV and HIV patent families and pending applications.

We hold the registered trademark PROCLEIX® and ULTRIO®, and the trademark OPTIVA . TIGRIS® is a trademark of Gen-Probe Incorporated.

Vaccines

FLUAD®, our adjuvanted influenza vaccine, contains the proprietary adjuvant MF59. The U.S. patents containing claims related to MF59 expire in 2018. Patents for MF59 in Canada, Japan, Germany, Ireland, Portugal and Hungary expire in 2010. Widely registered trademarks of Chiron and our subsidiaries include AGRIPPAL®, FLUAD®, FLUVIRIN®, MENJUGATE®, RABAVERT®, RABIPUR®, and RIBA®. Other trademarks of Chiron and our subsidiaries include BEGRIVAC , ENCEPUR , POLIORAL and TRIACELLUVAX .

Biopharmaceuticals

The patent family related to our first generation TOBI® tobramycin solution for inhalation product includes claims related to product formulation and methods of treating *pseudomonas aeruginosa* infections. The U.S. and European patents expire in 2014 and 2015, respectively.

We own or are the exclusive licensee of various patent families related to PROLEUKIN®, the serine-125 interleukin-2 mutein product, and uses thereof. The patents related to the PROLEUKIN® product will expire in the United States in 2012 and they expired in Europe in 2005.

One of the earliest patent families that relate to BETASERON® and BETAFERON® interferon beta-1b in the United States and Europe, respectively, relate to serine-17 interferon-beta protein used in manufacturing the product. The U.S. patent in this family expires in 2007. The terms of the European patent in this family has been extended to 2008 through Supplementary Protection Certificates.

We own additional pending patent applications directed to the use of IL-2 in combination therapy in cancer or infectious disease.

We own patent applications related to the use of tifacogin in severe pneumonia. Any eventual patent in this family will expire in 2022.

We have widely registered the trademarks PROLEUKIN® and TOBI® in addition to holding the trademark CARDIOXANE for dexrazoxane, a cardioprotectant for doxorubicin cancer treatment. The trademarks BETASERON® and BETAFERON® are trademarks of Schering AG. CUBICIN® is a trademark of Cubist Pharmaceuticals.

Seasonality

Sales of certain of our products, particularly influenza vaccines, are seasonal, with higher sales in the third and fourth quarters of the year. ENCEPUR , our vaccine against tick-borne encephalitis, is also seasonal with higher sales in the first half of the year.

Manufacturing and Raw Materials

Gen-Probe and Ortho-Clinical Diagnostics manufacture the products sold by our Blood Testing business segment. In the case of instrumentation, third party subcontractors perform manufacturing. We have engaged both Gen-Probe and Ortho-Clinical Diagnostics in extensive business continuity planning to limit any disruption to our current source of these blood safety products in the event of a loss of manufacturing capability. We maintain several months supply of NAT reagents in inventory. Ortho maintains similar inventories of immunodiagnostics products.

The vaccines segment primarily manufactures product in our facilities in the United Kingdom, Germany, Italy and India. In connection with the production of our influenza vaccine products, we must purchase large quantities of chicken eggs. For FLUVIRIN® vaccine, we purchase those eggs from a single supplier in the United Kingdom, and pursuant to the contract with that supplier we have agreed to make specified purchases from that supplier through 2012, subject to our right to terminate this agreement earlier upon payment of a termination fee.

Biopharmaceutical products are generally manufactured in our facilities in the United States. In addition, we perform some limited contract manufacturing for other organizations. Raw materials and supplies are generally available from various suppliers in quantities adequate to meet our needs, although we have single source suppliers for some components and value-add steps, including the pre-filled diluent syringe for BETASERON® interferon beta-1b. We purchase bulk powdered tobramycin, the primary basic raw material in TOBI® tobramycin, from two of the principal worldwide suppliers of the drug. We anticipate that either one of these suppliers alone will be able to supply sufficient quantities to meet current needs.

Our manufacturing facilities as well as those of our third-party service providers, suppliers and manufacturers are subject to continuing inspection by the FDA or comparable agencies in other jurisdictions.

We believe that our existing manufacturing facilities and outside sources will allow us to meet near-term manufacturing needs for our commercial products and our other products in clinical trials. In 2003, our Board of Directors approved $50.7 million in expenditures for a 25-year building lease and $42.2 million for capital improvements, both of which are part of a $97.0 million project for expansion and replacement of our influenza vaccines primary manufacturing facility in Liverpool, United Kingdom. The new manufacturing facility will replace a portion of the existing influenza vaccines manufacturing facilities in Liverpool, United Kingdom and is anticipated to be available in 2009 for the manufacture of influenza vaccines, subject to regulatory approval.

Employees

Our employees are the core of Chiron and are vital to our success. As of December 31, 2005, Chiron and its subsidiaries had approximately 5,500 employees, approximately 2,500 of whom were located in the United States. The company has experienced no work stoppages and we consider our employee relations to be good.

Relationship with Novartis AG

On October 30, 2005, Chiron entered into an Agreement and Plan of Merger (the Merger Agreement) with Novartis Corporation, Novartis Biotech Partnership, Inc. (Novartis Biotech), an indirect wholly owned subsidiary of Novartis AG (Novartis) and an indirect subsidiary of Novartis Corporation, and Novartis, as guarantor. Pursuant to the terms of the Merger Agreement, Novartis Biotech will merge with and into Chiron, with Chiron as the surviving corporation and becoming an indirect subsidiary of Novartis Corporation and an indirect wholly owned subsidiary of Novartis. Upon

completion of the merger, each share of Chiron common stock not held by Novartis or any of its subsidiaries, Chiron or any of its subsidiaries or a stockholder of Chiron who perfects appraisal rights, will be converted into the right to receive $45.00 per share in cash, without interest. The merger is subject to stockholder approval and satisfaction of other customary conditions, including governmental and regulatory approvals. On February 6, 2006, the European Commission adopted a decision pursuant to Article 6(1)(b) of the Council Regulation (EC) No. 139/2004 declaring the combination compatible with the common market. This follows approval by the U.S. Federal Trade Commission in December 2005 and clearance by the Committee on Foreign Investment in the United States under Exon-Florio in January 2006. We expect that the transaction will be completed in the second quarter of 2006.

Chiron and Novartis have been in an alliance since January 1995. We have entered into a series of agreements with Novartis, which provide, among other things and subject to certain conditions and exceptions:

- Novartis has the right to designate for nomination to our Board of Directors three individuals. The number of directors that Novartis may nominate declines if Novartis ownership interest in us is less than 30%.

- As long as Novartis owns at least 40% of our common stock, we may not engage in certain transactions, including significant debt or equity issuances, debt or equity repurchases, most mergers and acquisitions, the payment of cash dividends, amendments to Chiron s Restated Certificate of Incorporation or Bylaws, without Novartis approval.

- Novartis will not increase its ownership interest in us above 55% unless it either acquires all of our outstanding capital stock in a buy-out transaction or it increases its ownership interest in us up to 79.9% in a transaction approved by a majority of the independent members of our Board of Directors.

- Novartis provided certain funding to us for research on certain adult and pediatric vaccines, Insulin-like Growth Factor-I, Factor VIII gene therapy and Herpes Simplex Virus-thymidine kinase. Funding under this agreement ended December 31, 2001. In exchange for providing this funding, Novartis has certain co-promotion rights for certain vaccines and an interest in certain royalties on sales of certain products resulting from the funded research.

- Novartis will guarantee certain indebtedness on behalf of us until January 2008.

- Novartis has an option to purchase newly issued shares of our common stock directly from us at fair market value, subject to certain conditions, including the standstill restrictions described above.

- Novartis and we will cooperate and collaborate in research, development, manufacturing and marketing of biotechnology products on an arm s-length basis while remaining independent to pursue our respective corporate strategies and opportunities.

For more information on certain of these agreements, see Note 10, Related Party Transactions of Notes to Consolidated Financial Statements.

Available Information

The following documents can be found free of charge on our website at *http://www.chiron.com*, by contacting our Investor Relations department at (510) 923-2300 or by sending an e-mail message to *investor relations@chiron.com*:

- our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to these reports as soon as reasonably practicable after such filings are electronically filed with the Securities and Exchange Commission;

- our Corporate Governance Guidelines and our Code of Conduct and Commitment to Ethical Conduct; and

- the charters of the Audit Committee, Compensation Committee, Nominating and Corporate Governance Committee and Finance Committee of our Board of Directors.

The information contained on our website, or other websites linked to our website, is not part of and is not incorporated by reference into this report.

ITEM 1A. RISK FACTORS

We have discussed the most significant factors that may adversely affect our business and operations in Part II, Item 7, of this 10-K, Management s Discussion and Analysis of Financial Condition and Results of Operations, under the caption Factors That May Affect Future Results.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 2. PROPERTIES

Emeryville Campus

Our principal executive offices are located in Emeryville, California. As of December 31, 2005, our campus consisted of 24 buildings, of which 14 are leased and 10 are owned. Our Emeryville facilities include research and development, manufacturing and administrative facilities and a parking structure for our biopharmaceutical, vaccine and Blood Testing businesses.

Other Facilities

In 2003, our Board of Directors approved $50.7 million in expenditures for a 25-year building lease and $42.2 million for capital improvements, both of which are part of a $97.0 million project for expansion and replacement of our influenza vaccines primary manufacturing facility in Liverpool, United Kingdom. The new manufacturing facility will replace a portion of the existing influenza vaccines manufacturing facilities in Liverpool, United Kingdom and is anticipated to be available in 2009 for the manufacture of influenza vaccines, subject to regulatory approval.

We also own and lease manufacturing facilities in Vacaville, California used principally for our biopharmaceutical business. The owned facility has available capacity due to lower than expected demand for certain of our products and improved production yields from other facilities. As a result, we have entered into contract manufacturing agreements to utilize this available capacity (see the Biopharmaceuticals section in Part II, Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations below).

We have the following facilities for our vaccines operations:

Owned

- Manufacturing, administrative and development facilities in Rosia, Italy,

- Manufacturing, administrative and research and development facilities in Siena, Italy,

- Manufacturing facilities in Liverpool, United Kingdom and

- Manufacturing facilities in Ankleshwar, India.

Leased

- Manufacturing facilities in Liverpool, United Kingdom,
- Administrative office in Oxford, United Kingdom,
- Manufacturing, research and development and administrative facilities in Marburg, Germany,
- Administrative and sales offices in Mumbai, India,
- Sales office in Philadelphia, Pennsylvania,
- Sales office in Malaysia,
- Sales offices in Moscow, Russia,
- Sales offices in Szentendre, Hungary,
- Sales offices in Sao Paolo, Brazil,
- Sales office in China and
- Sales office in Brno-Slatina, Czech Republic.

We lease the following facilities for our biopharmaceutical operations:

- Research and development and administrative facilities in Seattle, Washington,
- Manufacturing and distribution facilities in Annandale, New Jersey,
- Administrative and sales offices in Amsterdam and Rijswijk, The Netherlands,
- Administrative and sales offices in Suresnes, France,
- Sales offices in Madrid, Spain,
- Sales offices in Lisbon, Portugal,
- Administrative and warehouse facilities in Munich, Germany,
- Sales offices in Milan, Italy,
- Sales and administrative offices in Dublin, Ireland,
- Sales offices in Quebec, Canada and
- Sales, marketing and administrative facility in Uxbridge, United Kingdom.

We lease sales and administrative offices for our Blood Testing operations:

- Suresnes, France and
- Hong Kong, China

We lease facilities in North America and Europe primarily for sales and service offices.

We believe that our other current facilities are in good operating condition and are adequate for our current needs. However, we are expanding to meet future requirements. We continually evaluate future requirements for our facilities.

ITEM 3. LEGAL PROCEEDINGS

Average Wholesale Price Litigation

In November 2004, the County of Nassau filed a complaint in the United States District Court for the Eastern District of New York against numerous biotechnology and pharmaceutical companies, including Chiron, in connection with setting average wholesale prices for various products, including TOBI® solution, which are reimbursed by Medicaid. In March 2005, the County of Nassau filed an amended complaint with the In Re Pharmaceutical Industry Average Wholesale Price Litigation pre-trial proceedings in the United States District Court for the District of Massachusetts. Plaintiff alleges that defendants violated federal racketeering laws, federal and state laws on Medicaid fraud, and state laws on unfair trade practice, breach of contract, fraud and unjust enrichment by devising and implementing a fraudulent pricing scheme against Medicaid beneficiaries, and seeks declaratory relief, as well as compensatory and punitive damages.

In February 2005, the State of Illinois through its Attorney General filed a complaint in the Circuit Court of Cook County, Illinois, County Department, Chancery Division, against numerous biotechnology and pharmaceutical companies, including Chiron, in connection with setting average wholesale prices for various products that are reimbursed by Medicare and Illinois Medicaid. The Attorney General alleges that defendants violated the Illinois Consumer Fraud and Deceptive Business Practices Act, the Illinois Public Assistance Fraud Act, and the Illinois Whistleblower Reward and Protection Act, and seeks declaratory relief as well as damages. In August 2005, the matter was transferred to the In Re Pharmaceutical Industry Average Wholesale Price Litigation in the United States District Court for the District of Massachusetts.

In June 2005, the City of New York and several New York State counties filed a complaint in the In Re Pharmaceutical Industry Average Wholesale Price Litigation in the United States District Court for the District of Massachusetts against numerous biotechnology and pharmaceutical companies, including Chiron, in connection with setting average wholesale prices for various products reimbursed by Medicaid, including TOBI®, PROLEUKIN®, and certain generic oncology drugs sold by the Cetus-Ben Venue Therapeutics partnership. Plaintiffs allege that defendants violated federal and state laws regarding Medicaid fraud, and state laws regarding social services fraud, health regulations, breach of contract, unfair trade practices, and unjust enrichment, and seek declaratory relief, as well as compensatory and punitive damages.

In October 2005, the State of Mississippi through its Attorney General filed a complaint in the Chancery Court of Hinds County, Mississippi, First Judicial District, against numerous biotechnology and pharmaceutical companies, including Chiron, in connection with setting average wholesale prices for various products that are reimbursed by Medicare and Mississippi Medicaid. The Attorney General alleges that defendants violated the Mississippi Medicaid Fraud Control Act, the Mississippi Regulation of Business for Consumer Protection Act, and certain Mississippi state common law provisions, and seeks declaratory relief as well as damages.

In November 2005, seven New York State counties filed complaints in the United States District Courts for the Northern, Southern and Western Districts of New York against numerous biotechnology and pharmaceutical companies, including Chiron, in connection with setting average wholesale prices for various products reimbursed by Medicaid, including TOBI® and certain generic oncology drugs sold by the Cetus-Ben Venue Therapeutics partnership. Plaintiffs allege that defendants violated federal and state laws regarding Medicaid fraud, and state laws regarding social services fraud, health regulations, breach of contract, unfair trade practices, and unjust enrichment, and seek declaratory relief, as well as compensatory and punitive damages.

It is not known when nor on what basis these matters will be resolved.

F. Hoffmann-La Roche A.G. and Roche Diagnostics GmbH HCV

In September 1999, F. Hoffman-LaRoche AG (Roche) filed an appeal with the Court of Appeals in Dusseldorf, Germany, regarding a Regional Court s decision to enjoin Roche from the import, use, possession and sale of certain hepatitis C virus immunoassay products in Germany based on Chiron s EP 0 318 216 (the 216 patent). After withdrawing certain claims from the 216 patent, Chiron rescinded that injunction and substituted EP 0 450 931 (the 931 patent) and Chiron s German Patent Nos. DD 298 527, DD 298 524 and DD 287 104 (collectively, the German Patents) in the appellate proceeding. In October 2003, the Court of Appeals ruled that Roche s HCV immunoassay kits containing a certain antigen infringe all three German Patents. Accordingly, the Court of Appeals granted Chiron requested injunction. Chiron has enforced the injunction. Roche is attempting to appeal this decision to the German Federal Supreme Court.

In July 2000, Chiron filed suit against Roche Diagnostics GmbH (Roche Diagnostics) in the German Federal Court (Landgericht) in Dusseldorf, Germany, asserting that Roche Diagnostics manufacture and sale of hepatitis C immunoassay products infringe Chiron s German Patent No. DD 298 524 (the 524 patent). In July 2003, the Landgericht decided that Roche Diagnostics HCV immunoassay kits containing a certain antigen infringe Chiron s 524 patent. Accordingly, the Landgericht granted Chiron the right to enjoin Roche Diagnostics from the import, use, possession and sale of such kits in Germany. In August 2003, Chiron enforced the injunction against Roche Diagnostics. In November 2003, Roche Diagnostics filed an appeal with the Court of Appeals. In January 2005, the Court of Appeals denied Roche Diagnostics appeal and denied Roche Diagnostics leave to appeal as a matter of right to the Supreme Court.

In December 2000, Roche Diagnostics initiated nullity proceedings before the German Federal Patent Court (Bundespatentgericht) regarding Chiron s 931 patent and the German Patents. In August 2002, the Bundespatentgericht upheld the validity of the German Patents, but nullified the German portion of the 931 patent. In November 2002, both Chiron and Roche Diagnostics filed appeals before the Federal Supreme Court regarding the Bundespatentgericht s nullity decisions. Certain infringement actions related to the 931, 104 and 527 nullity proceedings are currently stayed pending the outcome of these appeals.

It is not known when nor on what basis these matters will be resolved.

FLUVIRIN® influenza virus vaccine

For a discussion of developments related to FLUVIRIN® influenza virus vaccine, see Part II, Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, Factors That May Affect Future Results.

A. FLUVIRIN® vaccine Securities Class Actions

Between October 2004 and December 2004, five securities class action lawsuits were filed against Chiron and certain Chiron officers on behalf of purchasers of Chiron securities for class periods ranging from July 23, 2003 through October 13, 2004. Four of the suits were filed in the United States District Court for the Northern District of California. One action, although originally filed in the United States District Court for the Eastern District of Pennsylvania, was later transferred to the United States District Court for the Northern District of California. In March 2005, the Court named lead counsel and plaintiff, and in April 2005, lead plaintiff filed a consolidated complaint. The consolidated complaint alleges, among other things, that the defendants violated certain provisions of the federal securities laws by making false and misleading statements from July 23, 2003 through October 5, 2004 concerning the amount of FLUVIRIN® vaccine Chiron projected to produce and Chiron s historical and forecasted financial results,

and seeks unspecified monetary damages and other relief from all defendants. The trial is scheduled to begin on May 1, 2006.

B. FLUVIRIN® vaccine Shareholder Derivative Actions

Between October 2004 and November 2004, six shareholder derivative complaints were filed in the Superior Court of the State of California for the County of Alameda, naming Chiron as a nominal party and naming certain current and former Chiron officers and directors and Novartis AG as defendants in connection with the suspension of Chiron s license to manufacture FLUVIRIN® vaccine. One complaint also named Chiron as a defendant and sought relief from Chiron, including an equitable accounting. In December 2004, the six derivative actions were consolidated for discovery and trial under the caption In re Chiron Corporation Derivative Litigation (the Derivative Action). In February 2005, lead plaintiff filed a consolidated complaint, and in May 2005 filed an amended consolidated complaint alleging that defendants are liable for breach of their fiduciary duties of loyalty and care and other duties allegedly owed to Chiron in connection with Chiron s acquisition of its Liverpool, United Kingdom facility and the British regulatory agency s decision to suspend temporarily Chiron s license to manufacture FLUVIRIN® vaccine at the Liverpool facility, and seeking unspecified monetary damages and other relief from all defendants. The complaints did not seek any affirmative relief from Chiron. In July 2005, the Court granted without prejudice Chiron s and Novartis motions to dismiss the amended consolidated complaint based on three agreements entered in 1994 between Chiron and Novartis, all of which contain mandatory forum selection clauses requiring that any claims arising out of or relating to the agreements must be adjudicated in Delaware. Regarding the directors and officers, the Court also dismissed those claims implicated by the 1994 agreements, and stayed the remaining claims pending resolution of the action it is anticipated plaintiffs will file in Delaware. In September 2005, plaintiffs filed an appeal before the Superior Court of the State of California for the County of Alameda.

C. Other FLUVIRIN® vaccine Legal Matters

In October 2004, Chiron received a grand jury subpoena issued by the U.S. Attorney s Office for the United States District Court for the Southern District of New York requesting production of certain documents and materials relating to the suspension of our license. Also in October 2004, the U.S. Securities and Exchange Commission (SEC) notified Chiron that it would conduct an informal inquiry into the suspension with respect to potential violations of federal securities laws. The SEC also requested copies of related records. In February 2005, the SEC issued a formal order of investigation with respect to potential violations of federal securities laws. In February 2006, the SEC notified Chiron that it was terminating its investigation of whether Chiron violated any federal securities laws in connection with the previous suspension by the UK MHRA of Chiron s license to manufacture FLUVIRIN® influenza virus vaccine, and that no enforcement action would be recommended against the company.

In August 2005, Celltech Pharma (Celltech) filed a complaint against Chiron Vaccines and Chiron Behring GmbH & Co. KG (collectively, Chiron) in the Tribunal de Commerce of Nanterre in France. Celltech alleges that Chiron breached its alleged undertaking to provide FLUVIRIN® to Celltech for the 2004/2005 influenza season in France, and seeks damages.

It is not known when nor on what basis these matters will be resolved.

Institut Pasteur

In April 2003, Institut Pasteur filed a complaint in the United States District Court for the District of Columbia against Chiron seeking reversal of certain judgments entered by the Board of Patent Appeals and Interferences (the Board) of the United States Patent and Trademark Office in Patent Interference No. 103,659 (the 659 Interference). The 659 Interference involved claims in Chiron s U.S. Patent

No. 5,156,949 (the 949 patent) and in certain U.S. patent applications assigned to Institut Pasteur (the Chang applications), relating to HIV immunodiagnostic methods. In the 659 Interference, the Board decided that the inventors of Chiron s 949 patent were the first to invent the technology at issue. Chiron asserted that Institute Pasteur was barred from bringing claims per the 1993 HIV Cross-License Agreement between Chiron and Institut Pasteur (the Agreement), and that Institut Pasteur s standing to bring its appeal was a matter for arbitration under the terms of the Agreement. In February 2005, the Court ordered the parties to arbitrate the standing issue and the case was administratively dismissed. In March 2005, Chiron sent Institut Pasteur a notice of arbitration, and the arbitration commenced in January 2006.

It is not known when nor on what basis this matter will be resolved.

Investigation of Employees of Italian Subsidiary

Two sales employees of an indirect wholly owned Italian subsidiary of Chiron were the subject of an investigation by Italian authorities in Genoa, Italy in connection with a larger investigation into the purchasing activities of a Genoa hospital and alleged undue influence by the sales employees in the bidding process for the supply of blood testing products to the hospital. In August 2004, the hospital awarded Chiron a contract for the supply of blood testing products. Italian authorities also conducted an investigation in Milan, Italy concerning alleged corruption and undue influence by one of the sales employees implicated in the Genoa investigation. In February 2006, the Public Prosecutor of the Tribunal of Genoa concluded the investigation for the alleged offense of undue interference in public tenders, and has asked the Tribunal of Genoa to dismiss charges with respect to one of the employees. At this time, we are not aware of any investigation of Chiron with respect to these matters. Although Chiron is not the subject of any criminal charge, no assurance can be given that Chiron will not become the subject of civil charges, fines or penalties, or incur other damages or costs, in connection with these matters.

It is not known when nor on what basis these matters will be resolved.

Laboratory Corporation of America Holdings

In August 2003, Chiron filed a complaint in the United States District Court for the Northern District of California against Laboratory Corporation of America Holdings, Laboratory Corporation of America and National Genetics Institute (collectively, the Defendants), seeking damages and an injunction against Defendants manufacture, use and sale of certain HIV assays for infringing Chiron s U.S. Patent No. 6,531,276 (the 276 patent). In February 2004, Chiron voluntarily dismissed this case without prejudice and refiled the complaint before the United States District Court for the Central District of California. In April 2005, the Court stayed the case pending the outcome of two interferences declared by the U.S. Patent and Trademark Office regarding the 276 patent.

It is not known when nor on what basis this matter will be resolved.

Novartis AG Proposed Acquisition Shareholder Suits

Between September 1 and September 13, 2005, twelve class action lawsuits were filed by Chiron shareholders against Chiron, Novartis AG (Novartis), and members of Chiron s Board of Directors (collectively, the Defendants) regarding Novartis September 1, 2005 offer to acquire the approximately 58% of Chiron shares that Novartis does not already own for $40 per share (the Novartis Offer). Eight of the suits were filed in the Superior Court of the State of California in Alameda County (the California Court) by i) Ronald Abramoff, Harold Adelson, Beverly McCalla, Joan Weisberg, and David Jaroslawicz; ii) Edith Auman; iii) Joseph Fisher, MD, P.C. New Profit Sharing Trust, Trustee Joseph Fisher, MD; iv) William Lattarulo; v) Steven Rosenberg and The Harold Grill IRA; vi) Tracie Scotto; vii) Albert Stein; and viii) William Steiner (the California Plaintiffs). The remaining four suits were filed in the Court of

Chancery of the State of Delaware in and for New Castle County (the Delaware Court) by ix) Judy Longcore; x) Paulena Partners L.L.C.; xi) Sylvia Piven; and xii) the Thomas Stone Irrevocable Trust (the Delaware Plaintiffs). The eight California Actions were consolidated, as were the four Delaware Actions. In January 2006, the California Plaintiffs filed a consolidated complaint in the California Court, and in March 2006, the California Plaintiffs and certain of the Delaware Plaintiffs (together, Plaintiffs) filed a second amended consolidated complaint in the California Court against the Defendants alleging, among other things, that the Company and the Defendants breached their fiduciary duties in connection with the merger because the merger price is inadequate, unfair, and the result of an unfair process. The Plaintiffs also allege that Chiron s definitive proxy materials omit material information, include materially misleading statements and are unfairly coercive. In their prayer for relief, the Plaintiffs seek: (i) to enjoin the merger under the terms presently proposed; (ii) to rescind any transaction or be granted rescissory damages if a transaction is consummated prior to entry of final judgment; and (iii) to direct the individual defendants and Novartis to account to Plaintiffs and members of the purported class for all damages caused to them and to account for all profits and any special benefits obtained as a result of their alleged misconduct. A hearing on the California Plaintiff s anticipated motion for a preliminary injunction is currently scheduled for April 4, 2006.

It is not known when nor on what basis these matters will be resolved.

Senate Finance Committee Information Request

In June 2005, Chiron received a voluntary request for information from the U.S. Senate Committee on Finance (the Committee) in connection with the Committee s review of issues relating to the Medicare and Medicaid programs coverage of prescription drug benefits. The Committee requested information from Chiron as to our practices regarding educational grants. In January 2006, Chiron received a supplementary information request. Chiron, like the other pharmaceutical companies to whom the Committee has directed similar requests, is cooperating with the Committee.

It is not known when nor on what basis these matters will be resolved.

Sorin Biomedica/Snia

In January 2002, Chiron filed a complaint against Snia in the Court of Milan asserting that Snia s manufacture and sale of certain hepatitis C virus immunodiagnostics in Italy infringe the 931 patent. Chiron sought a declaration of infringement based on the 931 patent, as well as damages. In July 2005, the Court rejected Chiron s claims. This judgment is subject to appeal.

It is not known when nor on what basis these matters will be resolved.

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

No matters were brought to a vote of Chiron s stockholders in the quarter ended December 31, 2005.

EXECUTIVE OFFICERS OF THE REGISTRANT

The executive officers of Chiron are as follows, in alphabetical order:

Name	Age	Title
Ursula B. Bartels	48	Vice President; General Counsel and Secretary
Jack Goldstein	58	President and Chief Operating Officer
Anne Hill	46	Vice President, Human Resources
Jessica M. Hoover	48	Vice President; Head of Corporate Business Development
Meghan B. Leader	40	Vice President, Business Support Services and Chief Information Officer
Howard H. Pien	48	Chief Executive Officer and Chairman of the Board
Rino Rappuoli	53	Vice President; Chief Scientific Officer
David V. Smith	46	Vice President; Chief Financial Officer
Daniel B. Soland	47	Vice President; President, Chiron Vaccines
Bryan L Walser	40	Vice President, Corporate Strategy
Gene W. Walther	51	Vice President; President, Chiron Blood Testing
Craig A. Wheeler	45	Vice President; President, Chiron BioPharmaceuticals

Ms. Bartels joined Chiron as Vice President and General Counsel in August 2004. In March 2005, she was designated the Company s Secretary. Prior to joining Chiron, Ms. Bartels served as Vice President of Boehringer Ingelheim Corporation and Senior Vice President, General Counsel and Secretary of Boehringer Ingelheim Pharmaceuticals, Inc., where she was responsible for all legal functions for the corporation and its five U.S. subsidiaries. Boehringer s primary business focus was branded human pharmaceuticals (primarily respiratory) and multi-source pharmaceuticals (comprised of subsidiaries, Roxane Laboratories and Ben Venue Laboratories). Prior to joining Boehringer in 1999, Ms. Bartels worked at SmithKline Beecham Corporation (now GlaxoSmithKline) from 1988 to 1999, where she progressed from Counsel, Litigation to Vice President and Associate General Counsel, responsible for the full range of legal operations in North America for its two U.S. divisions, Pharmaceuticals, and Healthcare Services (including clinical laboratory and pharmacy benefit management businesses). Ms. Bartels was a member of the PhRMA Law Section Executive Committee from 1994 to 2004, and served as Chair of the Law Section in 2001-2002. Ms. Bartels assembled and led the group that wrote the PhRMA Code. Ms. Bartels began her legal career as a litigation associate at Stradley Ronan Stevens and Young, in Philadelphia. She graduated in 1979 from Bryn Mawr College, A.B. *cum laude*, and attended the University of Virginia School of Law, graduating in 1983.

Dr. Goldstein joined Chiron as Vice President and President, Chiron Blood Testing Division in September 2002. In February 2005, Dr. Goldstein was appointed to the position of President and Chief Operating Officer. He had served as interim Chief Operating Officer of Chiron since November 2004. From 2000 to 2002, Dr. Goldstein was General Partner at Windamere Venture Partners, L.L.C., a venture fund making investments in early stage biotechnology, pharmaceutical, medical device and diagnostic companies. From 1997 to 2001, Dr. Goldstein was President and CEO of Applied Imaging Corporation, a leading supplier of instrument systems for prenatal and cancer genetics. From 1999 until 2002, Dr. Goldstein also served as Chairman of the Board of Applied Imaging and continues to serve as a director of one of Applied Imaging s subsidiaries. From 1986 to 1997, Dr. Goldstein worked for Johnson & Johnson in various executive management positions, including President of Ortho Diagnostic Systems and Executive Vice President of Professional Diagnostics at Johnson & Johnson World Headquarters. Dr. Goldstein holds a B.A. degree in Biology from Rider University, an M.S. in Immunology and a Ph.D. in Microbiology from St. John s University.

Ms. Hill is responsible for human resources at Chiron. She joined Chiron in November 2004 from Baxter International Inc., where she served in a variety of executive positions of increasing responsibility from 1991 to 2004. From 1998 to 2004, she was global vice president of human resources for the Bioscience division of Baxter International in Westlake Village, California. Prior to relocating to the United States, Ms. Hill worked in human resources for the John Lewis Partnership, a large British retailer, from 1980 to 1990. Ms. Hill holds a BSc Econ degree in Industrial Relations from the University of Wales.

Ms. Hoover is responsible for corporate business development, including mergers, acquisitions, product licensing and other strategic transactions. She joined Chiron in 1994 as a member of the law department, most recently serving as vice president and assistant general counsel, where her responsibilities included strategic corporate transactions as well as business development initiatives within each of the company s business units. Before joining Chiron, Ms. Hoover was a partner with Brobeck, Phleger & Harrison. Ms. Hoover holds an A.B., with highest honors, from the University of California, Berkeley, and a J.D. from the Yale Law School.

Ms. Leader joined Chiron in 1992, and is the Vice President, Business Support Services and Chief Information Officer. She is responsible for information technology, corporate facilities, global security and corporate risk-mitigation services, including environmental health and safety, and business continuity planning. Since joining Chiron, Ms. Leader has held various positions in treasury, corporate development and information management. Prior to joining Chiron, she worked in treasury management for both Security Pacific Bank and Bank of America. Ms. Leader holds a B.A. degree in government and an M.B.A. from Saint Mary s College of California.

Mr. Pien joined Chiron as President and Chief Executive Officer, and a director, in April 2003. Upon the resignation of Seán P. Lance as Chiron s Chairman of the Board following the annual meeting of stockholders in May 2004, Mr. Pien also was elected Chairman of the Board. In February 2005, Mr. Pien s title of President was transferred to Dr. Goldstein in connection with the formalization of the role of Chief Operating Officer assumed by Dr. Goldstein. Mr. Pien joins Chiron from GlaxoSmithKline (GSK), which resulted from the merger of GlaxoWellcome and SmithKline Beecham, where he spent over twelve years in positions of international and global management responsibility, including: President of Pharmaceuticals International GSK from December 2000 to March 2003, including service as a member of the Corporate Executive Team; President, Pharmaceuticals, SmithKline Beecham (1998 to 2000); President, Pharmaceuticals-North America, SmithKline Beecham (1998); Senior Vice President and Director-North Asia (1997); Managing Director and Senior Vice President-UK (1995 to 1997); Vice President and Director, Marketing-US (1993 to 1995); Vice President and Director, Product Marketing-US, heading the arthritis, cardiovascular and vaccine groups (1992 to 1993); and Vice President and Director of New Product Development-US (1991 to 1992). Prior to joining SmithKline Beecham, Mr. Pien worked six years for Abbott Laboratories and five years for Merck & Co., in positions of sales, marketing research licensing and product management. Mr. Pien served as a director of ViroPharma Incorporated from 1998 to 2003. He currently serves as a director of two non-profit organizations: Oakland Children s Hospital and Bio-Tech Industry Trade Association.

Dr. Rappuoli joined Chiron as head of European vaccines research in 1992 with the acquisition of Italian vaccines company, Sclavo SpA, where he served as head of research and development. He was responsible for Chiron Infectious Disease and Vaccine Research, serving as Vice President, Vaccine Research, Research and Development from February 2000 to January 2004. At Chiron, he led the development of MENJUGATE® conjugate vaccine against meningococcus C and the first recombinant bacterial vaccine, against pertussis. In February 2004, he was promoted to Vice President, Chief Scientific Officer of Chiron. Dr. Rappuoli earned his doctoral and bachelor s degrees in biological sciences at the University of Siena, and also served as a visiting scientist at the Rockefeller University in New York and at the Harvard Medical School. Dr. Rappuoli is co-founder of the field of cellular microbiology, a discipline combining cell biology and microbiology, and has pioneered the genomic approach to vaccine development

termed reverse vaccinology . He is member of numerous international associations, including the European Molecular Biology Organization and the American Society for Microbiology. Dr. Rappuoli also has served on many committees, among which the NIH Search Committee for the Director of the Vaccine Research Center (Bethesda, Maryland). He is co-chairman of the R/D Task Force of the Global Alliance for Vaccines and Immunization. He has won several prestigious international awards including the Paul Ehrlich, Ludwig Darmstaedter Prize; and IUMS Arima award. Dr. Rappuoli currently serves as a director of Fondazione Monte Dei Paschi di Siena, a private organization in Siena, Italy. He was appointed as a foreign associate to the U.S. National Academy of Sciences in May 2005.

Mr. Smith joined Chiron as Vice President, Controller in February 1999 and was designated Chiron s principal accounting officer. In February 2002, Mr. Smith was appointed Vice President, Finance. In April 2003, Mr. Smith was appointed interim Chief Financial Officer. In November 2003, Mr. Smith was appointed Chief Financial Officer. Prior to joining Chiron, Mr. Smith served as the Vice President, Finance and Chief Financial Officer of Anergen, Inc. from 1997 until he joined Chiron. From 1988 to 1997, Mr. Smith held various financial management positions with Genentech, Inc., in both the United States and Europe.

Mr. Soland joined Chiron as Vice President and President, Chiron Vaccines in late February 2005. He is responsible for the operations of Chiron s global vaccine business. From 2003 until joining Chiron, Mr. Soland served as the President and Chief Executive Officer of Epigenesis Pharmaceuticals, a privately-held biopharmaceutical company that develops inhaled respiratory medicines for the treatment of asthma, chronic obstructive pulmonary disease and allergic rhinitis, from 2003 to 2005. From 1993 to 2003, Mr. Soland spent ten years with GlaxoSmithKline Biologicals in a variety of executive positions, including Vice President and Director, Worldwide Marketing Operations from 1998-2003, and Vice President and Director of SmithKline Beecham Pharmaceuticals, Vaccine Business Unit-U.S., from 1995 to 1998. Prior to joining GlaxoSmithKline, Mr. Soland spent eight years with Connaught Laboratories, a Pasteur Mérieux company with assignments in sales, sales management and product management. Mr. Soland holds a B.S. degree in Pharmacy from the University of Iowa, and was a licensed pharmacist (1981).

Dr. Walser joined Chiron as Division Vice President, Corporate Strategy in November 2001. Prior to joining Chiron, Dr. Walser was a principal in WRW, a Los-Angeles-based management consultancy working with The Rockefeller Foundation and the Boston Consulting Group on a variety of issues in biotechnology and healthcare. Before that, Dr. Walser trained in the Emergency Medicine program at UCLA, and worked for several years in Los Angeles with the healthcare practice of the Boston Consulting Group. Dr. Walser earned his undergraduate degree from Stanford, his medical degree from the University of Virginia School of Medicine and his law degree, *magna cum laude*, from Harvard Law School.

Mr. Walther initially joined Chiron as a consultant in August 1998, and was appointed as Vice President, Commercial Development, North America and Asia Pacific in January 2001. In February 2005, Mr. Walther was appointed to the position of President, Chiron Blood Testing. He had served as Acting President , Chiron Blood Testing since November 2004. Mr. Walther has over two decades of experience in the health care industry in various executive management positions. From 1995 to 1998, Mr. Walther was Vice President, Global Marketing and International Sales for Gen-Probe, Incorporated. From 1991 to 1995, Mr. Walther owned and operated a Seattle-based manufacturing company involved in producing equipment for the outdoor recreational industry. He was head of sales and marketing for Seattle-based Genetic Systems from 1984 to 1991. Prior to that, Mr. Walther worked for Abbott Diagnostics and American Hospital Supply Corporation in a variety of sales, marketing and business development positions. Mr. Walther holds a B.S. degree in microbiology and immunology from Michigan State University and a Masters of Business Administration from the University of Washington.

Mr. Wheeler joined Chiron as Vice President, President of Chiron BioPharmaceuticals, responsible for the commercial operations of Chiron s biopharmaceuticals business, in August 2001. Prior to joining Chiron, Mr. Wheeler was a senior member of The Boston Consulting Group s health care practice and a key contributor to the firm s practice in hospital strategy, disease management, and pharmaceutical capabilities. Based in Boston, he joined the firm in 1988. Before joining The Boston Consulting Group, Mr. Wheeler worked for Merck s MSDRL research unit, where he served as a senior engineer in process development. He recently served as the leader of The Boston Consulting Group s Scientist s Network. In partnership with the Rockefeller Foundation, he has joined the Global Alliance for TB Drug Development, a public-private partnership to develop new anti-tuberculosis drugs. Mr. Wheeler was appointed to the board of directors of Avanir Pharmaceuticals, an AMEX company, in September 2005.

PART II

ITEM 5. MARKET FOR THE REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is quoted on the NASDAQ National Market System under the symbol CHIR. As of December 31, 2005, there were 3,543 holders of record of Chiron common stock. We have declared no cash dividends since our inception and do not expect to pay any dividends in the foreseeable future. Pursuant to an agreement with Novartis, Novartis must approve our declaration and payment of dividends. See Relationship with Novartis AG above.

The quarterly high and low closing sales prices (rounded to the nearest one-hundredth) of our common stock for each quarter of 2005 and 2004 are shown below.

	2005		2004	
	High	Low	High	Low
First Quarter	$ 38.63	$ 32.61	$ 56.38	$ 44.01
Second Quarter	38.25	33.83	48.59	42.25
Third Quarter	44.34	34.96	48.01	42.38
Fourth Quarter	44.85	42.66	45.42	30.76

Our Board of Directors has, in the past, authorized the repurchase of our common stock on the open market through a stock repurchase program to offset the dilution associated with the issuance of new shares under the stock option and stock purchase plans and the granting of share rights. On December 5, 2003, the Board of Directors authorized Chiron to repurchase 5.0 million shares of Chiron common stock through December 31, 2004. Through December 31, 2004, we made purchases of 2.9 million shares, although there were no stock repurchases in the fourth quarter of 2004. On March 10, 2005, the Board of Directors authorized Chiron to repurchase 5.0 million shares of Chiron common stock through December 31, 2005. From January 1, 2005 through December 31, 2005 no shares were repurchased.

ITEM 6. SELECTED FINANCIAL DATA

We have derived the selected consolidated financial data presented below as of December 31, 2005 and 2004 and for the years ended December 31, 2005, 2004 and 2003 from the audited Consolidated Financial Statements contained elsewhere in this Form 10-K. The selected consolidated financial data presented below as of December 31, 2003, 2002 and 2001 and for the years ended December 31, 2002 and 2001 were derived from our audited Consolidated Financial Statements not contained herein. Operating results for the periods presented below are not necessarily indicative of the results that may be expected for future years.

	Year Ended December 31,				
	2005	2004	2003	2002	2001
	(In thousands, except per share data)				
Total revenues	$ 1,919,679	$ 1,723,355	$ 1,766,361	$ 1,276,280	$ 1,140,667
Income from continuing operations	180,470	54,063	220,338	181,145	174,758
Basic earnings per share from continuing operations	0.96	0.29	1.18	0.96	0.92
Diluted earnings per share from continuing operations	0.94	0.28	1.15	0.94	0.90
Total assets	4,747,479	4,305,503	4,195,169	2,960,344	2,866,909
Long-term debt and long-term portion of capital leases	1,047,606	1,093,604	1,084,386	416,954	408,696

As discussed in Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, several factors affected the comparability of information between 2005 and 2004. The first factor relates to our return of FLUVIRIN® product to the U.S. market for the 2005-2006 influenza season and our inability to release any FLUVIRIN® product during the 2004-2005 influenza season. Chiron had FLUVIRIN® vaccine sales of $96.5 million in late 2005 for the 2005-2006 influenza season but no FLUVIRIN® vaccine sales in 2004 (other than $2.3 million in late 2003-2004 season sales). In 2004, FLUVIRIN® cost of sales included a $91.3 million charge when Chiron wrote-off the entire inventory of FLUVIRIN® vaccine. In 2005, we incurred remediation costs associated with our Liverpool facility of $28.1 million and legal expenses of $16.6 million relating to the developments with respect to FLUVIRIN®, whereas in 2004, remediation costs and legal expenses were $2.6 million and $12.1 million, respectively. In addition, the amortization expense for the intangible assets associated with our acquisition of PowderJect was $37.0 million in 2005 and $54.7 million in 2004. Certain developed product technologies from Chiron s acquisition of PowderJect are amortized under the estimated sales method, which considers forecasted FLUVIRIN® sales during each influenza season through the remaining period of the benefit. Related amortization expense decreased in 2005 as compared with 2004, reflecting updated forecasted FLUVIRIN® sales. The second factor relates to our inability to release any BEGRIVAC product for the 2005-2006 influenza season. We reported no BEGRIVAC sales for 2005 versus $52.7 million of BEGRIVAC sales in 2004. In addition, we had to write off the existing BEGRIVAC product inventory, resulting in a charge of $18.0 million to cost of sales in 2005. Third, in 2005, we recognized an impairment loss of $14.5 million on acquired assets from PowderJect related to ARILVAX . Fourth, on June 12, 2004, certain holders of our Liquid Yield Option Notes (LYONs) tendered certain of the LYONs for purchase by Chiron. The aggregate purchase price for all the LYONs validly surrendered for purchase was $379.7 million. Fifth, in 2004, we issued $385.0 million aggregate principal amount of convertible debentures, which mature on June 30, 2034. Sixth, in December 2005, we received approximately $300.0 million, in connection with the sale of newly issued shares of our common stock to a subsidiary of Novartis. Under provisions of the 1994 Subscription Agreement with Novartis, as amended, Chiron exercised its right on October 30, 2005 to have Novartis purchase these shares.

As discussed in Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations, several factors affected the comparability of information between 2004 and 2003. The first factor relates to the effects of our acquisition of PowderJect on July 8, 2003 and developments with respect to FLUVIRIN® influenza virus vaccine, which impacted our results of operations in 2004. Chiron did not release any FLUVIRIN® product during the 2004-2005 influenza season. Chiron had no sales of FLUVIRIN® vaccine in 2004 (other than $2.3 million in late 2003-2004 season sales), while FLUVIRIN® vaccine sales were $219.2 million in 2003. In 2004, Chiron wrote-off the entire inventory of FLUVIRIN® vaccine, resulting in a $91.3 million charge to cost of sales, which decreased diluted earnings per share by approximately $0.36 in 2004. In 2004, Chiron incurred remediation costs associated with our Liverpool facility of $2.6 million and incurred legal expenses of $12.1 million related to the developments with respect to FLUVIRIN®, which together decreased diluted earnings per share by approximately $0.06 in 2004. In addition, we recorded a $45.3 million charge for purchased in-process research and development for the acquisition of PowderJect in 2003. The amortization expense for the acquired intangible assets associated with this acquisition was $54.7 million in 2004 and $25.3 million in 2003. Second, on June 12, 2004, certain holders of our LYONs tendered certain of the LYONs for purchase by Chiron. The aggregate purchase price for all the LYONs validly surrendered for purchase was $379.7 million. Third, we issued $385.0 million aggregate principal amount of convertible debentures, which mature on June 30, 2034. Fourth, on September 10, 2004, we reached a settlement agreement with F. Hoffman-La Roche regarding an HIV-related patent dispute. The impact on royalty and license fee revenue was $45.8 million. Fifth, on July 2, 2004, we acquired Sagres, a privately- held company headquartered in Davis, California, which focuses on the discovery and validation of targets with potential application to the development of

cancer therapeutics. We acquired Sagres for a preliminary purchase price of $12.0 million and allocated $9.6 million of the preliminary purchase price to purchased-in-process research and development, which we charged to earnings in 2004.

Factors that affected the comparability of information between 2003 and 2002 include (i) the effects of our acquisition of PowderJect in July 2003 which resulted in $244.7 million of additional revenues, as well as a $45.3 million charge for purchased in-process research and development in 2003 (the amortization expense for the acquired intangible assets associated with this acquisition was $25.3 million), (ii) we issued $500.0 million of convertible debentures in July 2003 and (iii) in July 2003, we entered into a new six-year lease to rent a research and development facility in Emeryville, California following the expiration of the existing operating lease. We accounted for this new lease as a capital lease and, as a result, recorded the leased facility and the corresponding liability on our balance sheet effective July 1, 2003. The amount recorded on the balance sheet for the leased facility was $157.5 million.

Factors that affected the comparability of information between 2002 and 2001 include (i) our implementation of Statement of Financial Accounting Standards (referred to as SFAS) No. 142 on January 1, 2002, which requires that assembled workforce be reclassified to goodwill and that goodwill (including assembled workforce) no longer be amortized, (ii) the commercial sale of the PROCLEIX® HIV-1/HCV Assay in the U.S in 2002 which was the primary contributor to an increase in worldwide product sales related to tests and instruments and the provision of services from $48.3 million in 2001 to $125.4 million in 2002 and (iii) our acquisition of Matrix Pharmaceutical, Inc. in 2002 for $67.0 million including a $45.2 million charge for purchased in-process research and development. The goodwill and assembled workforce amortization expense was $17.1 million in 2001.

See Note 18, Segment Information, of Notes to Consolidated Financial Statements for geographic information and operating results by operating segment.

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

Recent Developments

On October 30, 2005, we entered into an Agreement and Plan of Merger (the Merger Agreement) with Novartis Corporation, Novartis Biotech Partnership, Inc. (Novartis Biotech), an indirect wholly owned subsidiary of Novartis AG (Novartis) and an indirect subsidiary of Novartis Corporation, and Novartis, as guarantor. Pursuant to the terms of the Merger Agreement, Novartis Biotech will merge with and into our company, with our company as the surviving corporation and becoming an indirect subsidiary of Novartis Corporation and an indirect wholly owned subsidiary of Novartis. Upon completion of the merger, each share of our common stock not held by Novartis or any of its subsidiaries, our company or any of our subsidiaries or a stockholder of our company who perfects appraisal rights, will be converted into the right to receive $45.00 per share in cash, without interest. The merger is subject to stockholder approval and satisfaction of other customary conditions, including governmental and regulatory approvals. On February 6, 2006, the European Commission adopted a decision pursuant to Article 6(1)(b) of the Council Regulation (EC) No. 139/2004 declaring the combination compatible with the common market. This follows approval by the U.S. Federal Trade Commission in December 2005 and clearance by the Committee on Foreign Investment in the United States under Exon-Florio in January 2006. We expect that the transaction will be completed in the second quarter of 2006.

Immediately prior to signing the merger agreement, we gave notice to Novartis that we were exercising our right under the Subscription Agreement, dated as of November 20, 1994, as amended, with Novartis (as successor to Ciba-Geigy) to require Novartis or its affiliate to purchase shares of our common stock for an aggregate purchase price of $300.0 million at a per share purchase price of $43.50. On December 8, 2005, we closed on this sale.

On February 24, 2006 Schering AG notified Chiron of its intention to exercise its option under the Regulatory Filing, Development and Supply Agreement to purchase or lease all assets used by Chiron in the manufacture for Schering of BETASERON® interferon beta-1b products and all contractual rights at their fair market or lease value. The purchase/lease option is subject to the closing of the proposed acquisition of Chiron by Novartis AG. The agreement requires that the value be determined by an independent third party mutually agreed upon by both parties.

On March 16, 2006, we announced a recall and withdrawal of MORUPAR®, our measles, mumps and rubella (MMR) vaccine. We previously supplied MORUPAR® vaccine to customers in a limited number of developing countries, largely via the United Nations Children s Fund (UNICEF) and the Pan American Health Organization (PAHO), and to Italy. Results of pharmacovigilance surveillance in Italy suggest that MORUPAR® vaccine may be associated with a higher reported rate of adverse events following immunization than other MMR vaccine products. We expect to work with the World Health Organization (WHO) to assist it in conducting a risk-benefit analysis to determine whether UNICEF or PAHO will require a limited quantity of the existing inventory of MORUPAR® vaccine for their ongoing public health programs. We have written-off in 2005 approximately $6.0 million of MORUPAR® inventory as a result of the withdrawal and recorded approximately $1.7 million of product returns reserves in 2005 in connection with expected returns of 2005 product sales from the recall.

Introduction

We are a global biopharmaceutical company that participates in three healthcare markets: Blood Testing, vaccines, and biopharmaceuticals. Our revenues, which totaled $1.9 billion in 2005, consist of product sales, revenues from a joint business contractual arrangement, collaborative agreement revenues, royalty and license fee revenues and other revenues, primarily consisting of contract manufacturing and grant revenues. Our research and development efforts are focused on developing products for oncology and infectious and pulmonary disease.

Blood Testing

Our Blood Testing segment is dedicated to improving blood safety through the development and sale of novel blood-screening assays and equipment that protect the world s blood supply. Our Blood Testing segment, which reported total revenues of $555.7 million in 2005, is a world leader in nucleic acid testing, or NAT, blood screening with a leading position in the U.S, and a strong presence in Europe and Asia. The segment also generates revenues from a joint business contractual arrangement, a collaboration agreement, royalties and license fees.

Our Blood Testing segment consists of two separate collaborations: an alliance with Gen-Probe Incorporated (Gen-Probe) for NAT products, and a joint business contractual arrangement with Ortho-Clinical Diagnostics, Inc. (Ortho-Clinical Diagnostics) for immunodiagnostic products. Our collaboration with Gen-Probe was formed in 1998 and focuses on developing and commercializing NAT products to screen donated blood, plasma, organs and tissue for viral infection. We sell the collaboration s assays and instruments to blood banks under the PROCLEIX® brand name. Our joint business contractual arrangement with Ortho-Clinical Diagnostics was formed in 1989 to develop and sell immunodiagnostic tests to detect retroviruses and hepatitis viruses in blood. Ortho-Clinical Diagnostics manufactures and sells the assays and instrument systems. Chiron and Ortho-Clinical Diagnostics share equally in the profit of the contractual arrangement. Our Blood Testing segment also earns royalties and license fees from third parties based on their sales of immunodiagnostic and nucleic acid testing probe diagnostic products utilizing our hepatitis C virus and HIV-related patents, for use in blood screening and plasma fractionation markets.

Research and development is focused on programs to improve blood safety, including the development of an enzyme conversion system that converts groups A, B and AB red blood cells to enzyme-converted universal blood group O, and the development of a blood screening assay for variant Creutzfeldt-Jakob disease (vCJD).

Vaccines

Our vaccines segment is the fifth largest vaccines business in the world with total revenues of $602.1 million in 2005. We offer approximately 20 pediatric and adult vaccines including influenza, meningococcal, travel and pediatric vaccines. These vaccines have protected millions of people globally from potentially fatal diseases such as influenza, polio, rabies and meningococcal disease. We market our vaccines primarily in the United States, Germany, Italy and the United Kingdom.

Our heritage in vaccines is traced to the three European manufacturers we acquired over the past two decades, all of which were originally founded 100 or more years ago: Italy-based Sclavo was acquired in 1992, Germany-based Behring was acquired in 1998 and United Kingdom-based PowderJect Pharmaceutical plc, or PowderJect, was acquired in July 2003. We acquired FLUVIRIN® influenza virus vaccine as part of our acquisition of PowderJect.

Our vaccines segment research and development is focused on developing next generation influenza manufacturing capability, including our cell culture derived influenza vaccine, developing new vaccines for pandemic preparedness, and broadening our meningococcal franchise.

Biopharmaceuticals

Our biopharmaceuticals segment researches, develops, manufactures and markets a range of therapeutic products for cancer and infectious and pulmonary disease. The biopharmaceutical segment, which includes both product sales and royalties, reported total revenues of $629.0 million for the year 2005. Our marketed products include TOBI® tobramycin solution for inhalation, USP for pseudomonal lung infections in cystic fibrosis patients; PROLEUKIN® (aldesleukin) for injection for metastatic melanoma and renal cell carcinoma; and BETASERON® (interferon beta-1b) for subcutaneous injection for multiple sclerosis. In January 2006, the European Commission granted marketing approval to Chiron for CUBICIN® (daptomycin), a first-in-class IV antibiotic, adding another commercial product to our portfolio. The marketing approval was granted in the 25 member states of the European Union, Iceland, Liechtenstein and Norway. Under the approval, CUBICIN® is indicated for the treatment of complicated skin and soft-tissue infections (cSSTI) caused by Gram-positive bacteria. Research and development efforts are focused in the areas of oncology and infectious and pulmonary disease including the development of tobramycin inhalation powder, or TIP, a new tobramycin product with an enhanced method of delivery and the clinical advancement of tifacogin for the treatment of severe community-acquired pneumonia. Our oncology pipeline includes CHIR-258, a growth factor kinase inhibitor, CHIR-12.12, an anti CD-40 monoclonal antibody and CHIR-265, a Raf kinase inhibitor.

Royalties and License Fee Revenue

We earn royalty and license fee revenue in all three segments by licensing some of our key intellectual property in areas such as hepatitis C and HIV. In addition, we generate royalties through agreements with development and marketing partners, including royalties from Schering AG s sales of BETAFERON® (interferon beta-1b) in Europe. Some royalties and license fees are not considered to be associated with any particular business segment and are recorded separately in the segment data as Other Royalty and License Fee Revenues. Financial information for the reportable segments is included in Note 18, Segment Information of Notes to Consolidated Financial Statements.

We view certain other revenues and expenses as not belonging to any one segment. As a result, we have aggregated these items into an Other segment.

Influenza Virus Vaccines Recent Events

In October 2004, the U.K. regulatory body, the Medicines and Healthcare products Regulatory Agency, or MHRA, suspended our license to manufacture FLUVIRIN® at our Liverpool, U.K. facility. As a result of the suspension of our license, we did not release any FLUVIRIN® vaccine during the 2004-2005 influenza season. On March 2, 2005, the MHRA notified us that it had lifted the license suspension, giving Chiron clearance to initiate full production of FLUVIRIN® vaccine, conditioned on the understanding that Chiron s commitment to its remediation plan will continue and will be subject to further inspections by the MHRA.

On October 17, 2005 we initiated delivery and release of FLUVIRIN® vaccine to customers in the United States for the 2005-2006 influenza season. As of such time, we had received all necessary approvals from the U.S. Food and Drug Administration (FDA) and MHRA to start supplying FLUVIRIN® vaccine to the U.S. market.

We received a grand jury subpoena issued by the U.S. Attorney s Office for the Southern District of New York in October 2004 requesting production of certain documents relating to FLUVIRIN® vaccine and the suspension by the MHRA of our license. In February 2005, after having previously commenced an informal inquiry, the Securities and Exchange Commission, or SEC, notified us that it would commence a formal investigation into whether we or our employees violated any federal securities laws in connection with these developments regarding FLUVIRIN® vaccine, and Chiron subsequently received subpoenas from the SEC requesting production of certain documents relating to our Liverpool facility and FLUVIRIN® vaccine. In February 2006, the SEC notified us that it had decided to terminate its investigation, and that no enforcement action had been recommended against us. We also received a voluntary request for information from the United States House of Representatives, Energy and Commerce Committee, Subcommittee on Oversight and Investigations requesting production of certain documents. Numerous documents have been collected and produced in response to these requests, and several witnesses have been interviewed by the U.S. Attorney s Office, the SEC staff and Congressional staff. Additional investigations regarding these matters may arise.

In addition, we and certain of our officers and directors have also been named as defendants in several putative shareholder class action and derivative lawsuits alleging various claims arising out of or relating to these developments regarding FLUVIRIN® vaccine which are described above in Part I, Item 3, Legal Proceedings. Certain distributors and other parties with whom we had contracted to supply FLUVIRIN® vaccine are considering or have communicated claims against us as a result of our inability to supply FLUVIRIN® vaccine, and additional parties may do so in the future. On January 27, 2005, the U.S. Centers for Disease Control and Prevention, or CDC, terminated its contracts with us for the supply of FLUVIRIN® vaccine for default on the basis of our failure to supply such vaccine to the U.S. government for the 2004-2005 influenza season. The CDC has reserved the right to hold us liable for any excess costs it may have incurred in replacing any FLUVIRIN® vaccine that we failed to deliver and further has reserved all other remedies provided under the contract. It is not possible to predict whether any of these claims will be pursued and, if so, whether those claims will be upheld. Investigations, litigation and disputes have caused us to incur substantial expense and have required significant time and attention from our management and will continue to do so in the future and could result in civil action and/or criminal proceedings against us. The results of any such investigations, proceedings or disputes could have a material adverse effect on our consolidated financial position and results of operations and/or cash flow.

Although the MHRA has lifted its suspension of our license to manufacture FLUVIRIN® vaccine, we expect to incur additional expenses in connection with ongoing FLUVIRIN® vaccine matters, which could be material, including in connection with (1) our continuing remediation efforts at our Liverpool facility; and (2) responding to private lawsuits and other claims and investigations that exist or may arise.

BEGRIVAC vaccine is manufactured at our facility in Marburg, Germany. In July 2005, we reported that we would be unable to supply any BEGRIVAC vaccine doses for the 2005-2006 influenza season due to a product sterility issue and wrote off our existing product inventory resulting in charges of $18.0 million to cost of sales in 2005. Investigation of the product sterility issue has been completed and implementation of remedial measures and facility modifications is underway. Our inability to supply BEGRIVAC vaccine as planned to non-U.S. markets for the 2005-2006 influenza season or, if remedial efforts are delayed or not successful, future seasons could have a material adverse affect on our business and results of operations. In addition, it is possible that distributors and other parties with whom we had contracted to supply influenza vaccine may make claims against us as a result of Chiron not supplying influenza vaccine. Any such claims may cause us to incur substantial expense and require significant time and attention from our management. The results of any such claims could have a material adverse effect on our consolidated financial position and results of operations and/or cash flow.

Our previous inability to supply influenza vaccines has led to loss of market share and may lead to loss of additional market share in future seasons. Following the announcement of our FLUVIRIN® license suspension, competitors announced plans to introduce influenza vaccine products in the United States and sought expedited regulatory approval to do so. Even though the license suspension has been lifted, some of our customers may continue to choose to purchase influenza vaccine from other providers as their products become available in the United States. Loss of market share in the United States or foreign markets could have a material adverse effect on our business and results of operations. Delays in start-up procedures for ramping up to full production and normal manufacturing issues inherent in the complexity of influenza vaccine production had adversely affected the amount of FLUVIRIN® vaccine that we were able to produce for the 2005-2006 influenza season and may result in further loss of market share.

For additional information concerning the risks we face as a result of these influenza vaccine developments, see Factors That May Affect Future Results *Developments with respect to influenza vaccines over the past year may harm our business and results of operations.* For additional information on the U.S. Attorney s investigation, SEC investigation and private lawsuits and other claims, see Part I, Item 3. Legal Proceedings of this report on Form 10-K.

Summary Consolidated Financial Data

Following is an analysis and discussion of our operating results on a consolidated basis, which is followed by a description of our most critical accounting policies and use of estimates and more detailed analysis and discussion of our operating results by segment and our liquidity and capital resources.

	Year Ended December 31,			$ Change		% Change	
	2005	2004	2003	2005 vs. 2004	2004 vs. 2003	2005 vs. 2004	2004 vs. 2003
	($ in 000 s, except per share data)						
Product sales, net	$ 1,421,494	$ 1,268,303	$ 1,345,833	$ 153,191	$ (77,530)	12.1 %	(5.8)%
Revenue from joint business arrangement	136,701	118,246	108,298	18,455	9,948	15.6 %	9.2 %
Royalty and license fee revenues	317,006	289,561	250,142	27,445	39,419	9.5 %	15.8 %
Other revenues	31,394	29,201	43,526	2,193	(14,325)	7.5 %	(32.9)%
Total revenues	1,919,679	1,723,355	1,766,361	196,324	(43,006)	11.4 %	(2.4)%
Gross profit margin	48 %	47 %	58 %				
Research and Development expenses	433,891	431,128	409,806	2,763	21,322	0.6 %	5.2 %
Selling, general and administrative expenses	501,193	459,502	380,388	41,691	79,114	9.1 %	20.8 %
Purchased in-process research and development		9,629	45,300	(9,629)	(35,671)	(100.0)%	(78.7)%
Impairment loss on acquired intangible assets	15,658			15,658	-	100.0 %	
Income from continuing operations	180,470	54,063	220,338	126,407	(166,275)	233.8 %	(75.5)%
Diluted earnings per share from continuing operations	$ 0.94	$ 0.28	$ 1.15	$ 0.66	$ (0.87)	235.7 %	(75.7)%

2005 compared with 2004

Income from continuing operations was $180.5 million or $0.94 per diluted share and $54.1 million or $0.28 per diluted share in 2005 and 2004, respectively.

Income from continuing operations increased in 2005 as compared with 2004 primarily due to $96.5 million of FLUVIRIN® sales in 2005 for the 2005-2006 influenza season, a $91.3 million charge to cost of sales in 2004 resulting from the write-off of our entire FLUVIRIN® vaccine inventory in the third quarter of 2004 and $18.3 million lower amortization expense in 2005, primarily resulting from a revision of estimated future sales. In 2004, we did not have any FLUVIRIN® sales for the 2004-2005 influenza season. The lower amortization expense related to certain developed product technologies from our acquisition of

PowderJect, which are amortized under the estimated sales method over ten years. These factors were offset by a lost contribution from sales of BEGRIVAC influenza virus vaccine as there were no sales of BEGRIVAC vaccine in 2005 as compared with $52.7 million of sales in 2004, FLUVIRIN® vaccine remediation costs charged to cost of sales of $28.1 million in 2005 and $2.6 million in 2004, and the impairment loss in 2005 of $15.6 million on acquired intangible assets from our acquisition of PowderJect.

Revenues increased in 2005 as compared with 2004 primarily due to increased product sales, increased royalty and license fee revenue and increased revenues from the joint business arrangement. The change in total revenues was attributable in part to the movement in exchange rates, in particular the movements in the Euro and British Pound against the U.S. dollar. The movement in exchange rates had a minimal impact on total revenues in 2005. However, since our Euro and British Pound denominated expenses have also changed due to the movement in exchange rates, our income per share from continuing operations decreased $0.01 per diluted share in 2005, due to higher expenses compared with revenues denominated in Euros and British Pounds.

Product sales increased in 2005 as compared with 2004 primarily due to $96.5 million of FLUVIRIN® sales in 2005 for the 2005-2006 influenza season. In 2004, we did not have any FLUVIRIN® sales for the 2004-2005 influenza season. Product sales also increased due to increases in sales of our travel vaccines, PROCLEIX® product sales, TOBI® tobramycin, Meningococcal vaccines and BETASERON® interferon beta 1b. These increases were offset primarily by no sales of BEGRIVAC vaccine in 2005 as compared with $52.7 million of sales in 2004, and decreases in sales of our pediatric and other vaccines and PROLEUKIN® (aldesleukin).

Revenues from joint business arrangement increased in 2005 as compared with 2004 due to higher profitability realized by the joint business arrangement

Royalty and license fee revenues increased in 2005 as compared with 2004 primarily due to recognition of royalties from a settlement with a third party on patents owned by Rockefeller University, for which we are the exclusive licensee, increased BETAFERON® product royalties, increase in royalties from Roche for use of our patents in the blood screening and plasma fractionation markets and increase in royalties from our hepatitis C virus agreement with Roche. These increases are offset by $40.0 million in royalties relating to the September 2004 Roche settlement recognized in 2005, as compared with recognition of $46.0 million in the 2004.

In 2005, gross profit margin increased to 48% from 47% in 2004 primarily due to $96.5 million of FLUVIRIN® sales in 2005 for the 2005-2006 influenza season and a $91.3 million charge to cost of sales in 2004 resulting from the write-off of our entire FLUVIRIN® vaccine inventory in the third quarter of 2004. In 2004, we did not have any FLUVIRIN® sales for the 2004-2005 influenza season. These factors were offset by a lost contribution from sales of BEGRIVAC influenza virus vaccine as there were no sales of BEGRIVAC vaccine in 2005 as compared with $52.7 million of sales in 2004 and FLUVIRIN® vaccine remediation costs charged to cost of sales of $28.1 million in 2005 and $2.6 million in 2004.

Gross profit margins do not include amortization expense from acquired developed products, an intangible asset related to business combinations.

The main components of the increase in research and development expenses in 2005 as compared with 2004 relate to the cost of development efforts in our oncology, and meningococcal vaccine franchises, tifacogin and cell culture-derived influenza vaccine program. These increases were partially offset by research and development programs that had been discontinued prior to 2005.

The increase in selling, general and administrative expenses in 2005 as compared with 2004 was due to a broad range of activities including costs associated with the proposed merger between Chiron and Novartis AG, pre-launch costs for CUBICIN® daptomycin in Europe, higher employee-related costs, costs related to compliance with the Sarbanes-Oxley Act, and higher FLUVIRIN® vaccine-related legal costs.

The effective tax rate for 2005 was 11.0% of pretax income from continuing operations. The effective tax rate for 2004 was 28.2% of pretax income from continuing operations, including the charge for purchased in process research and development related to the Sagres acquisition, which was not tax deductible, and 25.0% of pre-tax income excluding such charge. The effective tax rate was higher in 2004 principally due to the impact of inter-company transfers of certain product rights in 2004, which increased foreign income taxes. There were no such transfers of product rights in 2005. Further, the effective tax rate in 2005 also includes increased benefits from state tax credits and certain foreign tax benefits which are, as a percentage of pre-tax income, higher than would be the case with higher levels of pre-tax income from FLUVIRIN® influenza vaccine sales. We do not consider this tax rate to be indicative of our effective tax rate going forward. The effective tax rate may be affected in future periods by changes in management s estimates with respect to our deferred tax assets and other items affecting the overall tax rate.

2004 compared with 2003

As described above, there were no sales of FLUVIRIN® vaccine for the 2004-2005 season. Sales of FLUVIRIN® influenza vaccine were $219.2 million for the year ended December 31, 2003. A contractual decline in the BETASERON® interferon beta-1b royalty rate, described in more detail below, resulted in a $34.8 million decline in total revenues for the twelve months ended December 31, 2004. Our total revenues were affected by the movement in exchange rates, in particular the movements in the Euro and British Pound against the U.S. dollar. The movement in exchange rates added approximately 3% to our total revenues for the twelve months ended December 31, 2004. As described above, we wrote-off our entire FLUVIRIN® product inventory, resulting in a $91.3 million charge to cost of sales, incurred remediation costs associated with our Liverpool facility of $2.6 million, and incurred legal expenses of $12.1 million related to the FLUVIRIN® vaccine developments discussed above under *Influenza Virus Vaccines Recent Events* , which decreased diluted earnings per share by approximately $0.42 for the twelve months ended December 31, 2004. Also since our Euro and British Pound denominated expenses have increased due to the movement in exchange rates, our earnings per share from continuing operations declined $0.08 per diluted share for the twelve months ended December 31, 2004, as our expenses denominated in Euros and British Pounds exceeded our revenues denominated in those currencies.

Product sales decreased in 2004 as compared with 2003 as there were no FLUVIRIN® influenza vaccine sales for the 2004-2005 season. The decrease in FLUVIRIN® vaccine sales was partially offset by increased sales in PROCLEIX® product sales, TOBI® tobramycin inhalation solution, other influenza vaccines products, PROLEUKIN® (aldesleukin) and travel vaccines. Sales of PROCLEIX® product sales and TOBI® tobramycin products increased 25% and 24%, respectively, in 2004 as compared with 2003.

Royalty and licenses fees increased significantly in 2004 compared with 2003 due to the Roche settlement regarding our HIV patent in the U.S. The settlement included a $78.0 million lump sum payment, of which $14.0 million was recognized in the third quarter 2004. In addition, the settlement resulted in $31.8 million of previously deferred royalty and license payments, being recognized in the third quarter 2004. The impact of these items from the Roche settlement was an approximate $0.18 increase in diluted earnings per share for 2004. Royalties and license fees also increased $7.9 million from a non-exclusive license we granted to the German Red Cross and $6.5 million from a licensing agreement with LabCorp.

Other revenues declined due to $14.4 million of revenue in 2003 from the Biogen and Serono settlements in connection with certain patents owned by Chiron and licensed exclusively to Schering AG s U.S. subsidiary, Berlex Laboratories.

In 2004, gross profit margin decreased to 47% from 58% in 2003, primarily due to the write-off of our entire inventory of FLUVIRIN® vaccine, resulting in a $91.3 million charge to cost of sales in the third quarter 2004, as well as the fact that there were no FLUVIRIN® vaccine sales for the 2004-2005 season. In addition, remediation costs of $2.6 million associated with our Liverpool facility were included in cost of sales in 2004. The effect of the FLUVIRIN® vaccine charge and remediation costs resulted in a 7 point decrease in our gross profit margin percentage in 2004. Gross profit margin was also negatively impacted by reduced sales and margins of the MENJUGATE® product, which decreased our gross profit margin by 2 percentage points when comparing 2004 with 2003.

Gross profit margins do not include amortization expense from acquired developed products, an intangible asset related to business combinations.

The main components of the increase in research and development expenses in 2004 as compared with 2003 include our infectious disease franchise, primarily tifacogin, our oncology franchise, our meningococcus vaccine franchise and our flu cell-culture program. These increases were partially offset by the discontinuance of development of tezacitabine and PA-2794. In addition, 2003 included expenses related to the in-licensing of CUBICIN® (daptomycin) and technology from ZymeQuest Inc. and Infectio Diagnostic Inc.

The increase in selling general and administrative expenses in 2004 as compared with 2003 mainly reflects an $18.0 million increase due to the movement in the Euro and British Pound exchange rates, $12.3 million from a full year of PowderJect expenses and $12.1 million in legal expenses related to the FLUVIRIN® developments discussed above under *Influenza Virus Vaccines Recent Events* . The remaining increase in selling, general and administrative expenses is primarily due to defense of our patents and technology, on-going marketing and pre-launch programs to support the continued growth of our business and investment in geographic penetration for our products and costs related to compliance with the Sarbanes-Oxley Act.

The effective tax rate for 2004 was 28.2% of pretax income from continuing operations, including the charge for purchased in process research and development related to the Sagres acquisition. The effective tax rate for 2003 was 28.7% of pretax income from continuing operations including the charge for purchased in-process research and development related to the PowderJect acquisition. The charges for the purchased in-process research and development in 2004 and 2003 are not tax deductible. The effective tax rates in 2004 and 2003 were both 25.0% of pretax income from continuing operations, after excluding the impact of the purchased in-process research and development charges. The effective tax rate in 2004 includes increased benefits from research tax credits and foreign income taxed at lower rates. Such benefits are a greater percentage of pretax income in 2004 than in 2003. These benefits were offset by the tax cost of transferring certain product rights through inter-company transactions as part of our long-term tax planning strategy. The effective tax rate may be affected in future periods by changes in management s estimates with respect to our deferred tax assets and other items affecting the overall tax rate.

Critical Accounting Policies and the Use of Estimates

The preparation of financial statements requires us to make estimates, assumptions and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to investments; inventories; derivatives; capital leases; intangible assets; goodwill; purchased in-process research and development; product discounts, rebates and returns; bad debts; collaborative, royalty and

license arrangements; restructuring; pension and other post-retirement benefits; income taxes; and litigation and other contingencies. We base our estimates on historical experience and various other assumptions that we believe to be reasonable under the circumstances, the results of which form our basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from those estimates under different assumptions or conditions.

Our Blood Testing segment includes our one-half share in the pretax operating earnings generated by the joint business contractual arrangement with Ortho-Clinical Diagnostics, Inc. Our joint business arrangement with Ortho-Clinical Diagnostics is a contractual arrangement and is not a separate and distinct legal entity. Through our joint business contractual arrangement with Ortho-Clinical Diagnostics, we sell a line of immunodiagnostic tests to detect hepatitis viruses and retroviruses and provide supplemental tests and microplate and chemiluminescent instrument systems to automate test performance and data collection. Prior to 2003, we accounted for revenues relating to non-U.S. affiliate sales on a one-quarter lag, with an adjustment of the estimate to actual in the subsequent quarter. More current information of non-U.S. affiliate sales of our joint business contractual arrangement became available in the first quarter 2003, and as a result, we are able to recognize revenues relating to non-U.S. affiliate sales on a one-month lag. The effect of this change, net of tax, was an increase to net income by $3.2 million for revenues from the joint business arrangement for the year ended December 31, 2003.

We believe the following critical accounting policies incorporate our more significant judgments and estimates used in the preparation of our Consolidated Financial Statements:

- Purchased in-process research and development We allocate the purchase price of acquisitions based on the fair value of the assets acquired and liabilities assumed. To assist in determining the value of the in-process research and development and certain other intangibles, a third party valuation is typically obtained as of the acquisition date if the acquisition is significant. We generally use the income approach to value in-process research and development. The income approach is based on the premise that the value of a security or asset is the present value of the future earning capacity that is available for distribution to the subject investors in the security or asset. We perform a discounted cash flow analysis, utilizing anticipated revenues, expenses and net cash flow forecasts related to the technology. Given the high risk associated with the development of new drugs, we probability adjust the revenue and expense forecasts to reflect the risk of advancement through the regulatory approval process based on the stage of development in the regulatory process. Such a valuation requires significant estimates and assumptions. We believe the fair value assigned to the in-process research and development is based on reasonable assumptions. However, these assumptions may be incomplete or inaccurate, and unanticipated events and circumstances may occur. Additionally, estimates for the purchase price allocation may change as subsequent information becomes available. For example, in the fourth quarter of 2003, upon completion of strategic assessments of the value of certain PowderJect research and development projects, we revised the allocation of a portion of the purchase price resulting in a $77.4 million decrease to purchased in-process research and development which we credited to operations and which was offset against goodwill.

- Investments We invest in marketable equity securities. The prices of some of our marketable securities are subject to considerable volatility. We record an impairment charge when we believe that an investment in a marketable security has experienced a decline in fair value, as measured by quoted market prices, that is other-than-temporary. Generally, we believe that an investment in a marketable security is impaired if its quoted market price has been below its carrying value for each trading day in a six-month period or a credit event has occurred, at which point we write down the investment. However, in determining whether impairment of a marketable security is considered to be other-than-temporary, we consider all available factors in the evaluation. These factors may

include, but are not limited to, (i) whether the issuer of the securities is experiencing depressed and declining earnings in relation to competitors, erosion of market share, and deteriorating financial position, (ii) whether the issuer is experiencing financial difficulties and its market is experiencing difficulties, (iii) ongoing activity in our collaborations with the issuer, if any, and (iv) the issuer s prospects for favorable clinical trial results, new product initiatives and new collaborative agreements. Decreases in the fair value of these securities may impact our profitability. To reduce this risk, we hedge a portion of our equity securities exposure through forward sales contracts.

- Inventories We maintain inventory reserves primarily for product failures, expiration and obsolescence. The manufacturing processes for many of our products are complex. Slight deviations anywhere in the manufacturing process may result in unacceptable changes in the products that may result in failures or recalls and, therefore, additional inventory reserves. Obsolete inventory, due to the expiration of shelf life, and the seasonal nature of some of our products, may result in additional inventory reserves. In estimating inventory obsolescence reserves, we analyze on a product-by-product basis (i) the shelf life and the expiration date, (ii) sales forecasts and (iii) inventory levels compared to forecasted usage. Judgment is required in determining whether the forecasted sales and usage information is sufficiently reliable to enable us to estimate an inventory obsolescence reserve. In addition, we operate in a highly competitive environment, with rapidly changing technologies. New technology or changes in production processes may result in product obsolescence. As a result, we may be required to record additional inventory reserves.

- Product returns and rebates We have extensive historical information on returns and rebates for our products. Historical information with respect to actual product returns and rebates is the primary factor assessed in estimating product returns and rebates allowances. In determining the allowance for product returns, we primarily use one of the following methodologies depending on the product: (i) we match the actual returns to the actual sale on a product-by-product basis to assess the historical trend for returns, and based on an analysis of the historical trend, the appropriate return percentage for the current period is then applied to current period sales to arrive at the product returns charge against revenue for the period or (ii) for seasonal products we analyze our actual returns over the previous seasons to arrive at the average actual returns percentage, which is then applied to the current season s sales to arrive at the charge against revenue for the current period. In estimating rebates, we use historical trends to analyze rebates against revenue on a product-by-product basis to arrive at an expected rebate percentage. This expected rebate percentage is applied to current period sales to arrive at the rebates expense for the period. If actual product returns and rebates vary, we may need to adjust our estimates and accruals accordingly.

- Collaborative, royalty and license arrangements We recognize up-front refundable fees as revenues upon the later of when they become nonrefundable or when performance obligations are completed. In situations where continuing performance obligations exist, we defer and amortize up-front nonrefundable fees ratably over the performance period, which is typically stipulated by the contract and we may also defer further until collection is reasonably assured. In arrangements with multiple deliverables, there may be significant judgment in determining whether the different revenue generating activities are separable. Milestones, if any, related to scientific or technical achievements are recognized in income when the milestone is accomplished. The terms of such arrangements may cause our operating results to vary considerably from period to period. We estimate royalty revenues based on previous period royalties received or on product sales forecast information provided by the third party licensee. In the subsequent quarter, we record an adjustment equal to the difference between those estimated royalty revenues recorded in the previous quarter and the contractual percentage of the third party s actual product sales for that

period. We exercise judgment in determining whether the forecast information provided by licensees is sufficiently reliable for us to base our royalty revenue recognition thereon.

- Income taxes Significant management judgment is required in developing our provision for income taxes, including the determination of deferred tax assets and liabilities and any valuation allowances that might be required against the deferred tax assets. We record valuation allowances to reduce deferred tax assets to the amounts that are more likely than not to be realized. We have considered future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for valuation allowances. If we determined that we would be able to realize our deferred tax assets in the future in excess of our net deferred tax assets, adjustments to the deferred tax assets would increase income by reducing tax expense in the period that we made such determination. Likewise, if we determined that we would not be able to realize all or part of our net deferred tax assets in the future, adjustments to the deferred tax assets would decrease income by increasing tax expense in the period that we made such determination. Annual tax provisions include amounts considered sufficient to pay assessments that may result from examination of prior year tax returns; however, the amount ultimately paid upon resolution of issues raised may differ materially from the amount accrued. In evaluating the exposure associated with various tax filing positions, we accrue charges for probable exposures. We maintain an allowance for tax contingencies, which management believes to be adequate. As part of our long-term tax planning strategy, we transfer certain product rights through inter-company transactions. Tax expense and the effective tax rate increase in the years these transactions take place, with the expected future benefit being lower taxation of future product revenues.

- Litigation and other contingencies We establish and maintain accruals for litigation and other contingencies when we believe a loss to be probable and reasonably estimable, as required by SFAS No. 5, Accounting for Contingencies. We base our accruals on information available internally within the company at the time of such determination and after management has consulted with and obtained advice from external professional advisors. Judgment is required in both the determination of probability and as to whether such an exposure is reasonably estimable. Information may become available to us after that time, for which adjustments to accruals may be required.

- Goodwill and intangible assets The valuation in connection with the initial purchase price allocation and the ongoing evaluation for impairment of goodwill and intangible assets requires significant management estimates and judgment. The purchase price allocation process requires management estimates and judgment as to expectations for various products and business strategies. If any of the significant assumptions differ from the estimates and judgments used in the purchase price allocation, this could result in different valuations for goodwill and intangible assets. For the PowderJect acquisition, we initially allocated $451.8 million of the purchase price to goodwill in the third quarter 2003. In the fourth quarter 2003, the allocation of the purchase price changed as we completed the strategic assessments of the value of certain research and development projects and adjusted the purchased in-process research and development, and upon finalization of certain estimates. Accordingly, goodwill associated with the PowderJect acquisition was adjusted to $503.0 million in the fourth quarter 2003. During 2004, we completed the planned divestiture of certain research operations in Madison, Wisconsin and Oxford, United Kingdom and certain vaccines operations in Sweden, we adjusted the previously recorded obligation related to an assumed defined benefit plan, revised estimates of exit costs associated with certain contractual obligations under supply and research agreements related to the divested research operations and other direct acquisition costs, and revised estimates of certain receivables and insurance estimates. The net impact of these items resulted in an increase to goodwill associated with the PowderJect acquisition of $17.9 million and goodwill was adjusted from $503.0 million in 2003 to $520.9 million

in 2004. Once it is established, we must test goodwill annually for impairment using a two-step process as required by SFAS No. 142, Goodwill and Other Intangible Assets. In addition, in certain circumstances, we must assess if goodwill should be tested for impairment between annual tests. Intangible assets with definite useful lives must be tested for impairment in accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. When we conduct our impairment tests for goodwill and intangibles, factors that are considered important in determining whether impairment might exist include significant continued under-performance compared to peers, significant changes in the underlying business and products of our reporting units, or other factors specific to each asset or reporting unit being evaluated. Any changes in key assumptions about the business and its prospects, or changes in market conditions or other externalities, could result in an impairment charge and such a charge could have a material adverse effect on our consolidated results of operations. For example, in the third quarter of 2005, we recognized an impairment loss of $14.5 million on acquired intangible assets from our acquisition of PowderJect related to ARILVAX , a yellow fever vaccine. This impairment loss was due to a focus of our resources towards the influenza market, resulting in a reduction of the expected activity for ARILVAX .

The accounting policies of our reportable segments are the same as those described in Note 1, The Company and Summary of Significant Accounting Policies, in the Notes to Consolidated Financial Statements.

Certain minor arithmetical variances between the following narrative and the Consolidated Financial Statements may arise due to rounding.

Results of Operations

Blood Testing

	Year Ended December 31,			$ Change		% Change	
	2005	2004	2003	2005 vs. 2004	2004 vs. 2003	2005 vs. 2004	2004 vs. 2003
	($ in 000 s, except percentages)						
Product sales, net:							
PROCLEIX® products	$ 273,407	$ 249,809	$ 200,066	$ 23,598	$ 49,743	9.4 %	24.9 %
Ortho-clinical Diagnostics	31,298	27,844	28,391	3,454	(547)	12.4 %	(1.9)%
	304,705	277,653	228,457	27,052	49,196	9.7 %	21.5 %
Revenue from joint business arrangement	136,701	118,246	108,298	18,455	9,948	15.6 %	9.2 %
Collaborative agreement revenues	7,222	8,044	9,012	(822)	(968)	(10.2)%	(10.7)%
Royalty and license fee revenues	106,045	89,192	75,407	16,853	13,785	18.9 %	18.3 %
Other revenues	1,031	979	466	52	513	5.3 %	110.1 %
Total Blood Testing revenues	$ 555,704	$ 494,114	$ 421,640	$ 61,590	$ 72,474	12.5 %	17.2 %
Gross profit margin	41 %	42 %	41 %				
Research and development expenses	$ 27,966	$ 29,238	$ 32,469	$ (1,272)	$ (3,231)	(4.4)%	(10.0)%
Selling, general and administrative expenses	$ 46,024	$ 41,885	$ 40,206	$ 4,139	$ 1,679	9.9 %	4.2 %

Product sales

PROCLEIX® Products On January 15, 2004, the PROCLEIX® ULTRIO® Assay for HIV-1/HCV/HBV received European CE marking for use on the semi-automated PROCLEIX® System, and on December 14, 2004, the PROCLEIX® ULTRIO® Assay received European CE marking for use on the fully automated, high throughput PROCLEIX® TIGRIS® System. Under a collaboration agreement with Gen-Probe, we market and sell the PROCLEIX® HIV-1/HCV Assay, the PROCLEIX® ULTRIO® Assay and related instrument systems. In addition to selling directly in the U.S., we also sell in various international markets, directly and through distributors. We record revenue based upon the reported results obtained from the customer from the use of assays to screen donations or upon sale and delivery of the assays, depending on the underlying contract. In the case of equipment sales or leases, we record revenue upon the sale and transfer of the title to the instrument or ratably over the life of the lease term, respectively. For the provision of service on the instruments, we recognize revenue ratably over the life of the service agreement.

The increase in product sales in 2005 as compared with 2004 was primarily due to (i) $20.6 million from the conversion to the PROCLEIX® ULTRIO® Assay from the PROCLEIX® HIV-1/HCV Assay outside the U.S. and from continued penetration into several markets abroad and (ii) $4.7 million from instrument sales and services in the U.S. These increases were partially offset by a $1.7 million decline in donations in the U.S.

The increase in product sales in 2004 as compared with 2003 was primarily due to (i) $19.6 million for the introduction of the West Nile Virus Assay on an investigational-use basis in the U.S. in March 2003, which had a full year of sales in 2004, (ii) $17.0 million for the continued penetration into several markets abroad and (iii) $10.4 million for market share gains in the U.S. for the PROCLEIX® HIV-1/HCV Assay.

Under a collaboration agreement with Gen-Probe, we market and sell the PROCLEIX® HIV-1/HCV Assay, the PROCLEIX® ULTRIO® Assay and related instrument systems. The Food and Drug Administration, or FDA, notified Gen-Probe on October 3, 2005 that it considers the PROCLEIX® TIGRIS® System not substantially equivalent to the enhanced semi-automated PROCLEIX® System (eSAS) for screening donated human blood with the PROCLEIX® ULTRIO® Assay. The FDA made this determination in response to Gen-Probe s 510(k) application for the TIGRIS system. Gen-Probe is in discussions with the FDA to resolve the outstanding issues.

Ortho-Clinical Diagnostics Under our joint business contractual arrangement with Ortho-Clinical Diagnostics, we manufacture bulk reagents and antigens and confirmatory test kits for immunodiagnostic products. The increase in 2005 as compared with 2004 primarily related to $3.5 million from the timing of manufacturing services under the arrangement for Ortho-Clinical Diagnostics. Sales in 2004 as compared with 2003 remained consistent. We also supply bulk antigens for Ortho-Clinical Diagnostics to be included in products to be sold by Bayer under a June 2001 agreement with Ortho-Clinical Diagnostics and Bayer Corporation (see also Royalty and license fee revenues Bayer below).

We expect competitive pressures related to our Blood Testing products to continue, primarily as a result of the introduction of competing products into the market, as listed in Part I, Item 1. Business Competition above.

Revenues from joint business arrangement The increase in revenue from the joint business arrangement in 2005 as compared with 2004 was primarily due to $19.6 million from higher profitability realized by the joint business arrangement offset by a decline of $2.2 million in royalties. The increase in revenue from joint business arrangement in 2004 as compared with 2003 was primarily due to (i) $9.8 million for higher profits from Ortho-Clinical Diagnostics U.S. operations and foreign affiliates and (ii) $5.3 million for an increase in royalties. These increases were partially offset by reorganization

charges from the joint business arrangement of $4.5 million and a one-time benefit of $4.3 million for the three months ended March 31, 2003 due to a change in estimate from a three-month lag to a one-month lag relating to non-U.S. affiliate sales. Prior to the first quarter of 2003, we accounted for revenues relating to Ortho-Clinical Diagnostics non-U.S. affiliate sales on a one-quarter lag. More current information is now available to us and as such, we now recognize revenues relating to non-U.S. affiliate sales on a one-month lag, consistent with the method of how we recognize revenues relating to Ortho-Clinical Diagnostics sales for the U.S. portion of Ortho-Clinical Diagnostics operations. For more information on this, see Critical Accounting Policies and the Use of Estimates.

Collaborative agreement revenues Collaborative agreement revenues tend to fluctuate based on the amount and timing of research services performed, the status of projects under collaboration and the achievement of milestones. Due to the nature of our collaborative agreement revenues, results in any one period are not necessarily indicative of results to be achieved in the future. Our ability to generate additional collaborative agreement revenues may depend, in part, on our ability to initiate and maintain relationships with potential and current collaborative partners.

Royalty and license fee revenues Our Blood Testing segment earns royalties from third parties based on their sales of immunodiagnostic and nucleic acid testing probe diagnostic products utilizing our hepatitis C virus (HCV) and HIV-related (HIV) patents, for use in the blood screening and plasma fractionation markets. Our Blood Testing segment also earns license fees related to our HCV and HIV patents for technologies used by third parties to develop products for use in the blood screening and plasma fractionation markets. Royalty revenues earned from diagnostic products are included in our other segment.

The increase in royalty and license fee revenues in 2005 as compared with 2004 was primarily due to (i) $13.5 million in royalties from the Roche settlement, (ii) $7.6 million in royalties from Roche due to rate increases resulting from certain countries entering the EU and an increase in reported donations, (iii) $7.0 million in fees and royalties from our licensing agreement with LabCorp, (iv) $6.3 million in license fees under our license agreements with the German Red Cross for the use of our hepatitis C virus (HCV) technology for use in molecular probe home brew blood screening and (v) $2.7 million from a settlement with the SNBTS regarding our HCV and HIV patents. These increases were partially offset by (i) $10.1 million recognized in the third quarter of 2004 for deferred revenues and a non-refundable portion of the Roche settlement reached in September 2004, as described below, (ii) $7.9 million in the third quarter of 2004 due to recognition of a portion of the license fee under our license agreements with the German Red Cross for the use of our HIV-1 and hepatitis C virus (HCV) technology for use in molecular probe home brew blood screening and (iii) $6.5 million in the fourth quarter of 2004 under our licensing agreement with LabCorp for our HCV intellectual property for nucleic acid testing (NAT).

The increase in royalty and license fee revenues in 2004 as compared with 2003 was primarily due to (i) $10.1 million for the settlement with Roche, as described below, (ii) $7.9 million due to recognition of a portion of the license fee under our license agreements with the German Red Cross for the use of our HIV-1 and HCV technology for use in molecular probe home brew blood screening and (iii) $6.5 million under our licensing agreement with LabCorp for our HCV intellectual property for nucleic acid testing (NAT). These increases were partially offset by a $7.0 million license fee from Baxter A.G. related to our HCV and HIV technology for use in the plasma fractionation market in 2003 and a $4.0 million one-time payment relating to back royalties, which was recognized in 2003.

Roche settlement In October 2000, we entered into three license agreements with Roche and several of its affiliated companies related to the settlement of certain litigation in the U.S. and certain other countries for the use of our hepatitis C virus and HIV nucleic acid testing intellectual property. Two agreements relate to *in vitro* diagnostic products. See Other Royalty and license fee revenues below. The third agreement relates to blood screening.

An HIV-related patent directed to nucleic acid testing methods for HIV-1 was issued in the U.S. on March 13, 2003. This patent will expire seventeen years from the date of issuance. As permitted under the terms of its licensing agreement, Roche decided to institute arbitration proceedings in regard to the application of the U.S. patent. Our Blood Testing segment had deferred recognition of royalties received and royalties accrued under the patent until the resolution of this dispute. On September 10, 2004, we reached a settlement agreement with Roche. Under the terms of the settlement agreement, royalties received prior to March 31, 2004 became non-refundable. For discussion regarding the impact of this settlement on our in vitro diagnostics products, see Other Royalty and license fee revenue below. Accordingly, in 2004, our Blood Testing segment recognized revenue of $5.5 million for royalties up until June 30, 2004, which had previously been deferred. Also under the settlement agreement, in 2005, we received a lump-sum payment of $78.0 million in lieu of royalties beyond January 1, 2005. For 2005, we recognized an aggregate of $40.0 million, with $26.5 million of revenue from this settlement recognized in our other segment and $13.5 million of revenue from this settlement recognized in our Blood Testing segment. Roche may elect under the terms of the agreement to obtain a partial refund and revert to paying royalties on the sales of its products in North America. The amount of such potential refund ranges between $64.0 million and $0.0 million. The amount of the refund available to Roche decreases in increments over the quarters of 2005 and 2006. As such, we are recognizing $64.0 million of the $78.0 million payment as revenue during 2005 and 2006. This revenue will be split between our Blood Testing segment and our other segment. The remaining $14.0 million is non-refundable and was recognized as revenue in 2004, of which, $9.3 million has been recognized as revenue in our other segment and $4.7 million has been recognized as revenue in our Blood Testing segment. We expect to recognize the remaining $24.0 million during 2006. Currently the applicable issued HCV-related patents expire in 2015 for the U.S. and in 2010 for Europe. The applicable issued HIV-related patent in Europe expired in October 2005.

Revenues under these blood screening agreements were $79.8 million, $69.0 million and $61.8 million in 2005, 2004 and 2003, respectively. The $79.8 million in 2005 includes $13.5 million of nonrefundable revenue under the September 10, 2004 settlement agreement with Roche, as discussed above. The $69.0 million in 2004 includes the $5.5 million of previously deferred revenue recognized in 2004 and the $4.7 million (for an aggregate of $10.1 million) of nonrefundable revenue recognized in 2004 under the September 10, 2004 settlement agreement with Roche, as discussed above. The impact on revenues in 2005 and 2004 from these items from the September 10, 2004 settlement with Roche is summarized under Other Royalty and license fee revenues below.

German Red Cross Settlement We have granted a non-exclusive license to the German Red Cross for use of our HIV-1 and HCV technology for use in molecular probe home brew blood screening through 2008. Of this license fee payment, $3.2 million and $7.9 million were recognized as royalty and license fee revenues in 2005 and 2004, respectively, and the remaining balance of $4.5 million is expected to be recognized through 2008, as the cancellation privilege in the related agreements expires. In addition, the German Red Cross has the option to license our patents beyond 2008 upon payment of an additional fee. In 2005 we recognized $6.3 million of revenue from the exercise of certain of these options by the German Red Cross. The licensing terms also cover potential past infringements.

LabCorp We have entered into a licensing agreement for our hepatitis C virus intellectual property for nucleic acid testing. The agreement gives LabCorp, including its subsidiary, National Genetics Institute, a semi-exclusive license to use our patented HCV NAT technology in screening plasma donations in the United States, subject to existing licenses and certain conditions. In 2004, we recognized a $6.5 million fee associated with this agreement. Revenue under this agreement was $7.0 million in 2005.

Scottish National Blood Service In 2005, we reached a $2.7 million settlement with the Scottish National Blood Transfusion Service regarding certain of our HCV and HIV patents which was recognized as revenue in 2005.

Baxter A.G. In June 2003, we entered into two license agreements with Baxter A.G. related to our HCV and HIV technology for use in the plasma fractionation market. Revenues under these agreements were $0.9 million, $1.3 million and $8.6 million in 2005, 2004 and 2003, respectively. We recognized a license fee of $7.0 million for these agreements in the second quarter 2003.

Bayer In June 2001, Chiron and Ortho-Clinical Diagnostics entered into an agreement with Bayer Corporation (Bayer) for the clinical diagnostic market. Under this agreement, Bayer manufactures and sells certain of Ortho-Clinical Diagnostics HCV and HIV immunodiagnostic products for use on Bayer s instrument platforms. Bayer paid us a license fee of $45.3 million, which we deferred (due to our continuing manufacturing obligations) and began recognizing as revenue in the third quarter 2001. We are recognizing the remaining amount ratably through 2010.

Royalty and license fee revenues may fluctuate based on the nature of the related agreements, the timing of receipt of license fees and the expiration of patents. Results in any one period are not necessarily indicative of results to be achieved in the future. Also, the license agreements typically provide for certain milestone payments and various royalties on future product sales if the licensee commercializes a product using our technology. However, we have no assurance that the licensee will meet their development objectives or commercialize a product using our technology. In addition, our ability to generate additional royalty and license fee revenues may depend, in part, on our ability to market and capitalize on our technologies.

Gross profit margin The decrease in gross profit margin in 2005 as compared with 2004 was primarily due to additional support and service costs associated with our fully automated, high throughput PROCLEIX® TIGRIS® System.

Gross profit margin increased in 2004 as compared with 2003 due to a positive impact by an adjustment to cost of goods sold in 2004 pursuant to our collaboration agreement with Gen-Probe. The Blood Testing gross profit margin benefited from an amendment in November 2003 to the worldwide blood screening collaboration agreement between Chiron and Gen-Probe in order to adopt permanent, fixed revenue shares for each party. Effective January 1, 2004, Gen-Probe s share was set at 45.75% of net revenues for assays, that include a test for HCV. For commercial assays, that do not test for HCV, such as the PROCLEIX® WNV Assay, the agreement remains unchanged with each party retaining 50% of the net revenues after deduction of specified expenses.

Blood Testing gross profit margin may fluctuate in future periods as the Blood Testing product and customer mix changes.

Research and development expenses The decrease in research and development expenses in 2005 as compared with 2004 was primarily due to $7.5 million decrease in costs relating to our nucleic acid testing products, partially offset by $6.2 million for research activities focused primarily on the development of an immunoassay to detect prions in blood that cause variant Creutzfeldt-Jakob disease.

The decrease in research and development expenses in 2004 as compared with 2003 was primarily due to (i) $6.5 million from purchased in-process technology associated with our investment in ZymeQuest, Inc. in 2003 (we are collaborating with ZymeQuest to develop and commercialize a enzymatic conversion system which converts group A, B and AB red blood cells to enzyme-converted group O (ECO®) red blood cells) and (ii) $2.6 million from costs associated with an agreement with Infectio Diagnostics Inc. in 2003, in which we licensed proprietary nucleic acid-based technology for the rapid detection of bacterial contamination in platelets and blood products. These decreases were partially offset by (i) $4.9 million due to the increased development efforts relating to nucleic acid testing products in 2004 and (ii) $1.0 million related to acquisition of in-process technologies in 2004, focused primarily on research into variant Creutzfeldt-Jakob disease.

Research and development expenses may fluctuate from period to period depending upon the stage of certain projects and the level of pre-clinical and clinical trial-related activities.

Selling, general and administrative expenses The increase in selling, general and administrative expenses in 2005 as compared with 2004 was primarily due to $2.5 million to support the geographic expansion of our customer base for the PROCLEIX® HIV-1/HCV Assay in international markets.

The increase in selling, general and administrative expenses in 2004 as compared with 2003 was primarily due to (i) $2.1 million from the support and pre-launch costs associated with the PROCLEIX® TIGRIS® System, a fully automated testing system and (ii) $1.6 million to support the geographic expansion of our customer base for the PROCLEIX® HIV-1/HCV Assay particularly in Latin America and Asia markets. These increases were partially offset by a decrease in other costs of $2.1 million.

We expect continued growth in selling, general and administrative expenses related to nucleic acid testing technology and products as our sales opportunities expand in new markets through anticipated additional nucleic acid testing adoption.

Vaccines

	Year Ended December 31,			$ Change		% Change	
	2005	2004	2003	2005 vs. 2004	2004 vs. 2003	2005 vs. 2004	2004 vs. 2003
	($ in 000 s, except percentages)						
Product sales, net:							
Influenza vaccines:							
Other Influenza vaccines (includes BEGRIVAC)	$ 128,900	$ 151,158	$ 113,188	$ (22,258)	$ 37,970	(14.7)%	33.5 %
FLUVIRIN® vaccine	96,455	2,255	219,240	94,200	(216,985)	4,177 %	(99.0)%
Influenza vaccines	225,355	153,413	332,428	71,942	(179,015)	46.9 %	(53.9)%
Meningococcal vaccines	43,361	27,739	65,548	15,622	(37,809)	56.3 %	(57.7)%
Travel vaccines	147,507	96,864	87,831	50,643	9,033	52.3 %	10.3 %
Pediatric and other vaccines	164,308	200,948	192,511	(36,640)	8,437	(18.2)%	4.4 %
	580,531	478,964	678,318	101,567	(199,354)	21.2 %	(29.4)%
Collaborative agreement revenues	4,328	8,646	4,222	(4,318)	4,424	(49.9)%	104.8 %
Royalty and license fee revenues	5,184	5,234	12,747	(50)	(7,513)	(1.0)%	(58.9)%
Other revenues	12,058	17,282	13,522	(5,224)	3,760	(30.2)%	27.8 %
Total vaccines revenues	$ 602,101	$ 510,126	$ 708,809	$ 91,975	$ (198,683)	18.0 %	(28.0)%
Gross profit margin	31 %	23 %	53 %				
Research and development expenses	$ 139,520	$ 135,380	$ 129,719	$ 4,140	$ 5,661	3.1 %	4.4 %
Selling, general and administrative expenses	$ 158,556	$ 158,569	$ 135,808	$ (13)	$ 22,761	(0.0)%	16.8 %
Amortization expense	$ 41,218	$ 59,519	$ 31,248	$ (18,301)	$ 28,271	(30.7)%	90.5 %
Impairment loss on acquired intangible assets	$ 15,658	$	$	$ 15,658	$	100 %	

Product sales We sell influenza, meningococcal, travel, pediatric and other vaccines. Our vaccines are sold in the U.S., Germany, Italy, the United Kingdom, as well as in other international markets.

Influenza vaccines As described above under *Influenza Virus Vaccines Recent Events,* as a result of recent developments with respect to FLUVIRIN® and BEGRIVAC vaccines, we had FLUVIRIN® vaccine sales of $96.5 million in 2005 and no BEGRIVAC vaccine sales in 2005. Sales of FLUVIRIN® influenza vaccine were $2.3 million in 2004 for late 2003-2004 influenza season and sales of BEGRIVAC influenza vaccine were $52.7 million in 2004. The decrease in sales of our other influenza vaccines is due to (i) no BEGRIVAC sales in 2005 and (ii) a manufacturing upgrade of facilities that produce influenza vaccine for the southern hemisphere. In 2004, sales of our other influenza vaccines to the southern hemisphere were $9.9 million. These decreases were partially offset by price increases for our other influenza vaccines.

In 2004, we had $2.3 million of FLUVIRIN® sales for late 2003-2004 season. Sales of FLUVIRIN® influenza vaccine were $219.2 million in 2003. Sales of our remaining influenza vaccines increased in 2004 as compared with 2003 primarily due to approximately $19.3 million for price increases and $11.2 million for the favorable movement in the Euro to U.S. Dollar exchange rate.

Meningococcal vaccines The increase in meningococcal vaccines sales in 2005 as compared with 2004 was primarily due to (i) $8.9 million increase in tender sales of MENJUGATE® vaccine in Spain, (ii) $7.8 million of MENZB meningococcal B vaccine sales to the Ministry of Health in New Zealand and (iii) a $1.8 million increase in tender sales of MENJUGATE® vaccine in Portugal. These increases are partially offset by a $2.7 million decrease in tender sales of MENJUGATE® vaccine in Australia and a $2.3 million decrease in tender sales of MENJUGATE® vaccine in the United Kingdom.

The decrease in meningococcal vaccines sales in 2004 as compared with 2003 was primarily due to a reduction of $51.1 million in sales of MENJUGATE® vaccine due to significant price erosion and reduced volume due to competition. This decrease was partially offset by sales in 2004 of $13.3 million of MENZB meningococcal B vaccine to the Ministry of Health in New Zealand.

Travel vaccines The increase in travel vaccines sales in 2005 as compared with 2004 was primarily due to: (i) a $27.8 million increase in tick-borne encephalitis (TBE) vaccine sales. Sales in the first quarter of 2004 were lower than in the first quarter of 2005 by $12.0 million due to $15.1 million of sales in the fourth quarter of 2003; TBE vaccines are typically sold in the first half of the year; and in addition, the second and third quarters of 2005 compared with the second and third quarters of 2004 reflected a $17.9 million increase in the TBE vaccine sales due to growth in the overall market and a number of marketing initiatives, (ii) $13.8 million from increased demand for our rabies vaccines in the U.S., primarily due to a product recall from a competitor and price increases, and increased sales to Canada, (iii) $7.5 million from increased demand for our rabies vaccines in Asia and (iv) $7.4 million from increased demand for our rabies vaccines in Europe, primarily due to tender sales to Turkey, Hungary and the U.K. These increases were partially offset by a decline of (i) $3.3 million due to a focus of our resources towards the influenza market and a reduction in activity for ARILVAX in 2005. ARILVAX remains in our portfolio of trademarks and we may re-enter the yellow fever vaccine market in the future with this product and (ii) $1.5 million in sales of Dukoral vaccine due to the divestiture in the second quarter of 2004 of certain vaccines operations in Sweden acquired in our acquisition of PowderJect.

The increase in travel vaccines sales in 2004 as compared with 2003 was primarily due to $25.7 million driven by increased demand for our rabies vaccines in the U.S., primarily due to a product recall from a competitor and increased demand of our rabies vaccines in Europe and Asia. The increase was partially offset by the fact that we had $15.1 million of sales of our tick-borne encephalitis vaccine in late 2003, which is typically sold in the first half of the year.

Pediatric and other vaccines Sales of our pediatric and other vaccines decreased in 2005 as compared with 2004 primarily due to (i) a $24.0 million decline in polio vaccines and measles, mumps and rubella vaccines sales due to product write-offs and a lack of product availability as a result of manufacturing upgrades, (ii) an $8.8 million decrease due to the timing of tender sales for our polio vaccines and measles, mumps and rubella vaccines, (iii) a $6.7 million decline due to the planned divestiture of certain vaccines operations in Sweden in the second quarter of 2004 acquired from our acquisition of PowderJect, (iv) a $14.5 million decrease from the interruption of production of certain vaccines in our Liverpool plant to focus on our remediation efforts at that plant and (v) a $1.7 million decrease due to product returns reserves in 2005 in connection with expected returns of 2005 product sales from the recall of MORUPAR®, our measles, mumps and rubella vaccine. These decreases were partially offset by a $19.2 million increase related to the timing of sales for diphtheria, tetanus and pertussis vaccines.

The increase in our pediatric and other vaccines sales in 2004 as compared with 2003 was primarily due to an additional $21.3 million related to the timing of tender sales for our polio vaccines and diphtheria, tetanus and pertussis vaccines, offset partially by (i) $7.3 million due to the planned divestiture of certain vaccines operations in Sweden in the second quarter 2004 acquired via our acquisition of PowderJect and (ii) $6.1 million due to the timing of tender sales for our measles, mumps and rubella vaccines.

Certain of our vaccine products are seasonal, particularly our influenza vaccines, which have higher sales primarily in the second half of the year. Our TBE vaccine is also seasonal with higher sales typically in the first half of the year. Certain of our vaccines require regulatory approval for production or sale of the product and sales may fluctuate depending on these regulatory approvals. We expect increased competition for our influenza vaccines business in the future as a result of the recent influenza vaccines developments. For more information on this, see *Influenza Virus Vaccines Recent Events* above. In addition, we expect MENJUGATE® vaccine sales to continue to fluctuate as public health authorities consider adoption of broad vaccination programs and competitive pressures continue to increase.

On October 27, 2005, we announced that we won a contract to supply the U.S. government with pre-pandemic influenza vaccine for a stockpile to protect against the H5N1 avian influenza virus strain. Under the agreement with the Department of Health and Human Services (HHS), we agreed to provide a bulk stockpile of H5N1 influenza vaccine, which we expect to produce at our Liverpool manufacturing facility using the U.S.-licensed commercial-scale manufacturing process. On February 24, 2006, we announced that the HHS had agreed to extend delivery terms for this stockpile. Prior to turning to seasonal FLUVIRIN® production, we had produced approximately 70% of the order. We expect to resume work on fulfilling the contract following completion of the FLUVIRIN® vaccine campaign in the fall. On February 24, 2006 we announced that we entered into a contract to supply the UK government with a stockpile of H5N1 influenza vaccine produced at our Siena manufacturing facility. Production of the H5N1 stockpiles vaccine under these agreements is not expected to affect production of our annual influenza virus vaccines. Delivery of the stockpile remains subject to internal and regulatory release procedures.

Collaborative agreement revenues We recognize collaborative agreement revenues for fees received as we perform research services and achieve specified milestones. Collaborative agreement revenues in 2005 as compared with 2004 decreased primarily due to $2.6 million in lower milestone payments related to an agreement to supply MENZB meningococcal B vaccine to the Ministry of Health in New Zealand.

Collaborative agreement revenues in 2004 as compared with 2003 increased primarily due to (i) $1.4 million in higher milestone payments related to an agreement to supply MENZB meningococcal B vaccine to the Ministry of Health in New Zealand and (ii) $3.0 million in increased collaborative agreement revenues following a full year of collaborative revenues in 2004 from our acquisition of PowderJect.

The balance of collaborative agreement revenues recognized in our vaccines segment consisted of various other arrangements, which individually were not material.

Collaborative agreement revenues tend to fluctuate based on the amount and timing of research services performed, the status of projects under collaboration and the achievement of milestones. Due to the nature of our collaborative agreement revenues, results in any one period are not necessarily indicative of results to be achieved in the future. In addition, the collaboration agreements typically provide for certain milestone payments and various royalties on future product sales if the collaborative partners commercialize a product using our technology. Also, our ability to generate additional collaborative agreement revenues may depend, in part, on our ability to initiate and maintain relationships with potential and current collaborative partners.

Royalty and license fee revenues Our vaccines segment earns royalties on third party sales of, and license fees on, several products.

GlaxoSmithKline An agreement with GlaxoSmithKline plc provides for royalties on sales of certain vaccine products. Under this agreement, we recognized $3.2 million, $2.9 million and $7.1 million of such royalties in 2005, 2004 and 2003, respectively. Royalties were consistent between 2005 and 2004. The decrease in royalties in 2004 compared with 2003 was primarily due to the expiration of various patents under this agreement.

Other In 2005, 2004 and 2003, we recognized $0.9 million, $1.0 million and $5.6 million, respectively, of royalty revenues primarily on third party sales of hepatitis B virus vaccine products. Certain patents related to the production of hepatitis B vaccine products expired beginning in 2004, which resulted in reductions in royalty revenues recognized under one arrangement.

The balance of royalty and license fee revenues recognized in our vaccines segment consisted of various other arrangements, which individually were not material.

Royalty and license fee revenues may fluctuate based on the nature of the related agreements, the timing of receipt of license fees and the expiration of patents. Results in any one period are not necessarily indicative of results to be achieved in the future. Also, the license agreements typically provide for certain milestone payments and various royalties on future product sales if the licensees commercialize a product using our technology. However, we have no assurance that the licensee will meet their development objectives or commercialize a product using our technology. In addition, our ability to generate additional royalty and license fee revenues may depend, in part, on our ability to market and capitalize on our technologies.

Other revenues

Grant and contract revenues Our vaccines segment other revenues included grant and contract revenues of $10.0 million, $13.4 million and $9.7 million in 2005, 2004 and 2003, respectively. We have entered into a series of agreements with the U.S. National Institutes of Health to advance our HIV vaccine program into human clinical trials. We recognized grant and contract revenues under these arrangements of $6.1 million, $8.1 million and $7.3 million in 2005, 2004 and 2003, respectively.

The balance of other revenues consisted of various other agreements, which individually were not material.

Other revenues recognized in our vaccines segment may fluctuate due to the nature of the revenues recognized and the timing of events giving rise to these revenues.

Gross profit Gross profit margin increased in 2005 as compared with 2004 primarily due to $96.5 million of FLUVIRIN® vaccine sales in 2005 for the 2005-2006 influenza season and a $91.3 million charge to cost of sales resulting from the write-off of our entire FLUVIRIN® vaccine inventory in the third quarter of 2004. In 2004, we did not have any FLUVIRIN® vaccine sales for the 2004-2005 influenza

season. These factors were partially offset by (i) a lost contribution from sales of BEGRIVAC influenza virus vaccine as there were no sales of BEGRIVAC vaccine in 2005 as compared with $52.7 million of sales in 2004, (ii) an $18.0 million charge for the write-off of BEGRIVAC product inventory due to product sterility issues, (iii) FLUVIRIN® vaccine remediation costs charged to cost of sales of $28.1 million in 2005 and $2.6 million in 2004, (iv) a decline in sales of our Polio and MMR vaccines due to lack of product availability as a result of manufacturing upgrades, (v) $19.1 million charged to cost of sales in 2005 due to the write-off of certain FLUVIRIN® vaccine inventory primarily due to normal manufacturing issues and excess finished product and semi-finished product at the end of the season and (vi) $6.0 million charged to cost of sales in 2005 due to the write-off of MORUPAR® inventory as a result of the withdrawal.

Gross profit margin declined in 2004 as compared with 2003 primarily due to (i) the fact that there were no FLUVIRIN® vaccine sales for the 2004-2005 influenza season and (ii) a $91.3 million charge to cost of sales resulting from the write-off of our entire inventory of FLUVIRIN® vaccine. In addition, 2004 included approximately $2.6 million in FLUVIRIN® vaccine remediation costs, which were charged to cost of sales. Gross profit margin was also negatively impacted by reduced sales and margins of the MENJUGATE® product. These factors were offset by higher prices of our other influenza vaccines products and increased sales of our rabies vaccine in the U.S. market.

Vaccines gross profit margin does not include amortization expense from acquired developed products, an intangible asset related to business combinations. Such amortization expense is included in the caption amortization expense of intangible assets acquired in business combinations and asset purchases discussed below.

Vaccines gross profit margin may fluctuate significantly in future periods due to product and customer mix, seasonality and ordering patterns, production yields, regulatory approvals and competitive pressures.

Research and development expenses The increase in research and development expenses in 2005 as compared with 2004 was primarily due to $8.3 million from advancing our quadrivalent meningococcal vaccine candidate for serogroups A,C,W and Y, and $4.8 million from our flu cell culture development program. These increases were partially offset by $7.2 million for our Phase III trial for MENJUGATE® meningococcus C vaccine in the United States in 2004, with no comparable spending in 2005, and the second quarter of 2004 divestiture of certain research and development operations, acquired in the acquisition of PowderJect. The divested operations included $4.2 million in research and development expenses in 2004.

The increase in research and development expenses in 2004 as compared with 2003 was primarily due to (i) $7.3 million from flu cell culture and (ii) $7.1 million from the advancement of several programs in our meningococcal franchise. These increases were mainly offset by the effects of the planned divestiture of certain research operations, associated with our acquisition of PowderJect, in Madison, Wisconsin and Oxford, United Kingdom during the second quarter of 2004. Research and development expense associated with these operations in 2004 as compared with 2003 decreased $8.8 million.

In 2004, we successfully concluded our Phase III trial for MENJUGATE® meningococcus C vaccine in the United States. We will not be filing a Biologics License Application for the vaccine and instead focus our resources on advancing our quadrivalent meningococcus vaccine candidate for serogroups A,C,W and Y.

Research and development expenses may fluctuate from period to period depending upon the stage of certain projects and the level of pre-clinical and clinical trial-related activities.

Selling, general and administrative expenses The decrease in selling, general and administrative expenses in 2005 as compared with 2004 was due to (i) a reduction of $4.1 million as a result of the planned

divestiture of certain PowderJect operations in the second quarter 2004, (ii) $3.0 million from the recovery of bad debt and (iii) $4.5 million from reductions in marketing activities. These decreases were partially offset by increases of (i) $2.8 million due to the movement in the Euro and British pound to U.S. Dollar exchange rate, (ii) an additional $3.4 million for costs related to compliance with the Sarbanes-Oxley Act, (iii) an additional $2.5 million from the establishment of sales and marketing operations in the U.S., (iv) $2.4 million for executive severance and (v) an additional $1.7 million of personnel costs.

The increase in selling, general and administrative expenses in 2004 as compared with 2003 was primarily related to additional expenses of $12.3 million attributable to our third quarter 2003 PowderJect acquisition. The remaining increase in selling, general and administrative expenses resulted from $12.5 million from the movement of the Euro and British Pound to U.S. dollar exchange rates and $9.4 million associated with ongoing sales and marketing programs. These were partially offset by savings of $4.5 million from the divestiture of certain PowderJect research and development operations in 2004.

Amortization expenses The decrease in amortization expense in 2005 as compared with 2004 was due to lower amortization expense related to certain developed product technologies from our acquisition of PowderJect, which are amortized under the estimated sales method. The estimated sales method considers forecasted FLUVIRIN® sales during each influenza season through the remaining period of the benefit. Related amortization was $34.2 million as compared with $48.2 million in 2005 and 2004, respectively reflecting updated forecasted FLUVIRIN® sales. The increase in amortization expense in 2004 as compared with 2003 primarily related to the intangible assets acquired following our third quarter 2003 PowderJect acquisition.

Impairment loss on acquired intangible assets In 2005, we recognized an impairment loss of $14.5 million on acquired intangible assets from our acquisition of PowderJect related to ARILVAX , a yellow fever vaccine. This impairment loss was due to a focus of our resources towards the influenza market, resulting in a reduction of the expected activity for ARILVAX . ARILVAX remains in our portfolio of trademarks and we may re-enter the yellow fever vaccine market in the future with this product. In addition, in 2005, we recognized an impairment loss of $1.1 million on acquired intangible assets from our acquisition of PowderJect related to a contract manufacturing agreement. This impairment loss was due to a reduction of the expected activity for this contract manufacturing agreement.

Biopharmaceuticals

	Year Ended December 31,			$ Change		% Change	
	2005	2004	2003	2005 vs. 2004	2004 vs. 2003	2005 vs. 2004	2004 vs. 2003
	($ in 000s, except percentages)						
Product sales, net:							
BETASERON® interferon beta-1b	$ 142,238	$ 130,572	$ 124,936	$ 11,666	$ 5,636	8.9 %	4.5 %
TOBI® tobramycin	232,624	212,876	172,047	19,748	40,829	9.3 %	23.7 %
PROLEUKIN® (aldesleukin)	123,549	129,377	115,075	(5,828)	14,302	(4.5)%	12.4 %
Other	37,847	38,861	27,000	(1,014)	11,861	(2.6)%	43.9 %
	536,258	511,686	439,058	24,572	72,628	4.8 %	16.5 %
Collaborative agreement revenues	1,534	1,354	5,328	180	(3,974)	13.3 %	(74.6)%
Royalty and license fee revenues	72,950	71,527	87,698	1,423	(16,171)	2.0 %	(18.4)%
Other revenues	18,305	10,940	29,538	7,365	(18,598)	67.3 %	(63.0)%
Total biopharmaceuticals revenues	$ 629,047	$ 595,507	$ 561,622	$ 33,540	$ 33,885	5.6 %	6.0 %
Gross profit margin	72 %	72 %	72 %				
Research and development expenses	$ 266,405	$ 266,511	$ 247,618	$ (106)	$ 18,893	(0.0)%	7.6 %
Selling, general and administrative expenses	$ 148,453	$ 142,114	$ 117,505	$ 6,339	$ 24,609	4.5 %	20.9 %
Amortization expense	$ 24,988	$ 24,984	$ 25,117	$ 4	$ (133)	0.0 %	(0.5)%

Product sales Biopharmaceutical product sales in 2005, 2004 and 2003 consisted principally of BETASERON® interferon beta-1b, TOBI® tobramycin and PROLEUKIN® (aldesleukin) products.

BETASERON® interferon beta-1b We manufacture interferon beta-1b which is marketed by Schering AG and its affiliates, including Berlex Laboratories, Inc. (collectively Schering), under the trade names BETASERON® (in the U.S and other non-European markets) and BETAFERON® (in Europe). Boehringer Ingelheim also supplies BETAFERON® interferon beta-1b to Schering for sale in Europe. For product we manufacture, we recognize a portion of revenue for product sales upon shipment to Schering and the remainder based on a contractual percentage of sales by Schering, both of which we record as product sales. For product manufactured by Boehringer Ingelheim and marketed by Schering in Europe under the trade name BETAFERON®, we receive royalties calculated at the same percentage of sales less the amount paid or incurred by Schering for supply costs, which we record in royalty and license fee revenues. Starting in the fourth quarter 2003, the amount we record as product sales and BETAFERON® royalties, based on a percentage of sales by Schering, declined by five percentage points pursuant to our contractual agreement with Schering. As a result, the percentage of sales per unit on which our payments are based has decreased, reducing our per unit revenue by approximately 18% (for sales of Chiron product) and approximately 34% (for royalties from sales of Boehringer Ingelheim product) from that received prior to the decline. However, there are a number of mitigating considerations, including (i) the transitional supply agreement and (ii) the volume mix of Chiron product and Boehringer Ingelheim product. We believe these considerations have partially offset this contractual change.

In October 2003, the U.S. Food and Drug Administration approved a new pre-filled diluent syringe for BETASERON® interferon beta-1b. The pre-filled diluent syringe was launched in January 2004 and enhances the delivery mode and shortens preparation, helping to simplify injections of BETASERON®

interferon beta-1b. In the first quarter 2003, the U.S. Food and Drug Administration approved new labeling for BETASERON® interferon beta-1b. The labeling expands the indication for BETASERON® interferon beta-1b to treat all relapsing forms of multiple sclerosis to reduce the frequency of clinical exacerbations. Relapsing forms of multiple sclerosis include relapsing-remitting, the most common form, and secondary progressive multiple sclerosis with relapses.

Pursuant to our agreement with Schering, we began supplying BETAFERON® product to Schering in the fourth quarter 2002 for certain additional European markets, which were previously supplied by Boehringer Ingelheim. This resulted in a shift of revenue recognized under this agreement to product sales, and a decrease in royalty revenues beginning in the fourth quarter 2002. In 2003, Schering extended its supply agreement with Boehringer Ingelheim through 2008. The exact shift of revenue in the future will be contingent on our production capacity, Schering s minimum purchase commitment under the extended supply agreement with Boehringer Ingelheim, and market demand. The shift to product sales is expected to increase over the next three years. We expect overall, biopharmaceutical earnings to be largely unaffected by the transition. In order to supply BETAFERON® to Schering, we are required to make capital improvements to our existing manufacturing facilities to increase capacity. During 2005, 2004 and 2003, we recorded charges related to process development and test runs associated with this project. See Research and development expenses below.

The increase in BETASERON® product sales in 2005 as compared with 2004 primarily related to (i) $8.4 million from price increases and (ii) $5.0 million from a shift of revenue from royalties to product sales as Schering began to sell product manufactured by us in additional European markets. These increases were partially offset by (i) $3.1 million from reduced shipments to Berlex and (ii) $0.9 million from inventory ordering patterns.

The increase in BETASERON® product sales in 2004 as compared with 2003 primarily related to an additional (i) $7.5 million from price increases, (ii) $4.2 million from increased patient demand attributed to key marketing programs, (iii) $3.2 million from the benefit of foreign exchange rates, (iv) $6.1 million from inventory ordering patterns of Schering and their distributors and (v) $2.9 million from increased sales of clinical materials. These increases were partially offset by an $18.5 million reduction due to a decline in the royalty rate by five percentage points pursuant to our contractual agreement with Schering.

On February 24, 2006 Schering AG notified Chiron of its intention to exercise its option under the Regulatory Filing, Development and Supply Agreement to purchase or lease all assets used by Chiron in the manufacture for Schering of BETASERON® interferon beta-1b products and all contractual rights at their fair market or lease value. The purchase/lease option is subject to the closing of the proposed acquisition of Chiron by Novartis AG. The agreement requires that the value be determined by an independent third party mutually agreed upon by both parties.

TOBI® tobramycin solution for inhalation We sell TOBI® solution directly in the U.S. and certain international markets. The increase in sales in 2005 as compared with 2004 was primarily due to (i) $15.9 million due to price increases and (ii) $12.5 million due to increased patient demand in both the United States and Europe. These increases were partially offset by $7.5 million reduction due to inventory ordering patterns and $0.8 million for a government rebate adjustment.

The increase in sales in 2004 as compared with 2003 was primarily due to (i) $16.0 million in increased patient demand in the U.S, (ii) $9.2 million in price increases, (iii) $6.4 million in favorable movement in the Euro to U.S. Dollar exchange rate and (iv) $6.0 million in inventory ordering patterns.

We continue to seek approval of TOBI® solution in other countries. Inventory ordering patterns of our wholesalers and distributors as well as reimbursement and government pressures, competition, foreign currency exchange rates and the level of rebates may influence future TOBI® product sales. In

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December 2002, the U.S. Food and Drug Administration tentatively approved an abbreviated new drug application for an inhaled tobramycin for sale in the U.S. following expiration of the orphan drug status of the TOBI® solution in December 2004. Subsequently, the application was withdrawn and under terms of a settlement agreement reached in October 2003, approval will not be sought to market this generic product until the 2014 expiration of our patent in the U.S. covering the formulation of TOBI® solution for inhalation.

PROLEUKIN® (aldesleukin) The decrease in PROLEUKIN® (aldesleukin) product sales in 2005 as compared with 2004 was primarily due to (i) $10.7 million due to a decrease in patient demand as a result of increased competition and (ii) $1.6 million for a government rebate adjustment. These decreases were partially offset by $6.6 million for price increases.

The increase in sales for PROLEUKIN® (aldesleukin) product sales in 2004 as compared with 2003 was primarily due to (i) $8.0 million from inventory ordering patterns in Europe, (ii) $5.2 million from price increases and (iii) $3.0 million due to favorable movement in the Euro to U.S. Dollar exchange rate. These increases were partially offset by a $4.2 million reduction due to a decline in patient demand.

The balance of product sales recognized in our biopharmaceuticals segment consisted of various other products, which individually were not material.

Inventory ordering patterns, reimbursement and government pressures, competition, foreign currency exchange rates and the level of rebates may influence future biopharmaceutical sales.

Collaborative agreement revenues We recognize collaborative agreement revenues for fees received as we perform research services and achieve specified milestones.

Collaborative agreement revenues tend to fluctuate based on the amount and timing of research services performed, the status of projects under collaboration and the achievement of milestones. Due to the nature of our collaborative agreement revenues, results in any one period are not necessarily indicative of results to be achieved in the future. In addition, the collaboration agreements typically provide for certain milestone payments and various royalties on future product sales if the collaborative partners commercialize a product using our technology. Also, our ability to generate additional collaborative agreement revenues may depend, in part, on our ability to initiate and maintain relationships with potential and current collaborative partners.

Royalty and license fee revenues Our biopharmaceuticals segment earns royalties on third party sales of several products, including BETAFERON® interferon beta-1b and recombinant insulin and glucagon products. Our biopharmaceuticals segment also earns license fees for technologies, such as hepatitis C virus-related patents, used by third parties to develop therapeutic products.

BETAFERON® interferon beta-1b BETAFERON® product royalties were $60.0 million, $51.6 million and $63.8 million in 2005, 2004 and 2003, respectively.

The increase in BETAFERON® product royalties in 2005 as compared with 2004 was primarily due to (i) $5.4 million from an increase in demand and (ii) $3.9 million from price increases. These increases were partially offset by $4.4 million from a shift of revenue from royalties to product sales as Schering began to sell product manufactured by us in additional European markets.

The decrease in 2004 as compared with 2003 was primarily due to $16.6 million from the reduction in the royalty rate of five percentage points, pursuant to our contractual agreement with Schering, partially offset by (i) $5.2 million due to favorable movement in the Euro to U.S. Dollar exchange rate and (ii) $4.6 million due to an increase in demand.

As discussed in Product sales *BETASERON® interferon beta-1b* above, we began supplying BETAFERON® product, which was previously supplied by Boehringer Ingelheim, to Schering in the fourth quarter 2002 for certain additional European markets. This resulted in a shift of revenue recognized under this agreement to product sales, with a decrease in royalty revenues, beginning in the fourth quarter 2002. In 2003, Schering extended its supply agreement with Boehringer Ingelheim through 2008. The magnitude of the shift of revenue in the future will be contingent on our production capacity, Schering s minimum purchase commitment under the extended supply agreement with Boehringer Ingelheim and market demand. The shift to product sales is expected to increase over the next three years. Future BETAFERON® product royalties will be influenced by demand, price changes and foreign currency exchange rates.

Novo Nordisk We earn royalty revenues on insulin and glucagon product sales by Novo Nordisk AS. We recognized $3.8 million, $4.4 million and $8.5 million in 2005, 2004 and 2003, respectively, under these arrangements. Patents related to the production of insulin and glucagons began expiring in late 2003, and as a result, there were significant reductions in royalty revenue in 2005 and 2004 recognized under these arrangements. We expect royalties under these arrangements to continue to decrease as certain U.S. patents expire in 2006 and 2007.

The balance of royalty and license fee revenues recognized in our biopharmaceuticals segment consisted of various other agreements, which individually were not material.

Royalty and license fee revenues may fluctuate based on the nature of the related agreements, the timing of receipt of license fees and the expiration of patents. Results in any one period are not necessarily indicative of results to be achieved in the future. Also, the license agreements typically provide for certain milestone payments and various royalties on future product sales if the licensees commercialize a product using our technology. However, we have no assurance that the licensees will meet their development objectives or commercialize a product using our technology. In addition, our ability to generate additional royalty and license fee revenues may depend, in part, on our ability to market and capitalize on our technologies.

Other revenues

Contract manufacturing revenues Our biopharmaceuticals segment recognized contract manufacturing revenues of $17.1 million, $10.3 million and $13.5 million in 2005, 2004 and 2003, respectively. The fluctuations in 2005 as compared with 2004 and in 2004 as compared with 2003 resulted from the level of activity and the timing of contract manufacturing activities.

Biogen and Serono settlements As a result of a favorable federal court decision and prior agreements between Chiron and Schering s U.S. subsidiary, Berlex Laboratories, and Berlex and Biogen, Biogen was required to make a settlement payment to Schering. In accordance with an earlier contract between Chiron and Berlex, we recognized approximately $13.0 million as revenue in 2003, which represented our share of this settlement payment. In addition, there was a similar settlement between Berlex and Serono, S.A. of which we recognized approximately $1.4 million in 2003.

The balance of other revenues recognized in our biopharmaceuticals segment consisted of various other arrangements, which individually were not material.

Other revenues recognized in our biopharmaceuticals segment may fluctuate due to the nature of the revenues recognized and the timing of events giving rise to these revenues. There can be no assurance that we will be successful in obtaining additional revenues or that these revenues will not decline.

Gross profit margin The biopharmaceutical gross profit margin in 2005 was consistent with the gross profit margin in 2004. The effect of price increases were offset by costs associated with a planned increase in idle time for manufacturing facilities and ongoing process improvement efforts.

The biopharmaceutical gross profit margin in 2004 was consistent with the gross profit margin in 2003. The effect of price increases were offset by the lower royalties from the contractual change in the royalty rate related to the sale of BETASERON® product and the increased costs associated with the pre-filled diluent syringe for BETASERON® product.

Biopharmaceutical gross profit margin does not include amortization expense from acquired developed products, an intangible asset related to business combinations. Such amortization expense is included in the caption amortization expense of intangible assets acquired in business combinations and assets purchases.

Biopharmaceutical gross profit margin may fluctuate significantly in future periods due to production yields, increased cost to produce the BETASERON® interferon beta-1b pre-filled diluent syringe and as the biopharmaceutical product and customer mix changes.

Research and development expenses The decrease in research and development expenses in 2005 as compared with 2004 was primarily due to (i) a $14.2 million decrease in expenses related to the SILCAAT trial, as discussed below, (ii) a $5.0 million decrease in expenses for the development of PULMINIQ (cyclosporine, USP) inhalation solution and (iii) a $3.0 million decrease related to the discontinued development of tezacitabine in the first quarter of 2004 based on an analysis of the data from a Phase II trial in patients with gastro esophageal cancer. These decreases are partially offset by increased expenditures of (i) $8.6 million for the progression of phase I clinical studies of our oncology compound CHIR-258 (small molecule), (ii) $5.3 million for activities related to the development of tifacogin, (iii) $1.1 million for development activities related to CUBICIN® (daptomycin) for treatment of complicated skin and soft tissue infections, (iv) $1.6 million related to the development of new processes and performance of test runs related to installed equipment of our existing manufacturing facilities to support the supply of BETAFERON® interferon beta-1b to Schering and (vi) $1.5 million for development of tobramycin inhalation powder.

The increase in research and development spending in 2004 as compared with 2003 was primarily the result of (i) $30.7 million from activities related to the development of tifacogin, as discussed below, (ii) $15.2 million from development of our early-stage oncology compounds CHIR-258 (small molecule) and CHIR 12.12 (an antibody) and (iii) $7.1 million from pre-registration activities for PULMINIQ (cyclosporine, USP) inhalation solution for the increase in survival and prevention of chronic rejection in patients receiving allogenic lung transplants, in combination with standard immunosuppressive therapy. These increases were partially offset by (i) a reduction of $13.5 million due to the discontinued development of tezacitabine in the first quarter of 2004 based on an analysis of the data from a Phase II trial in patients with gastroesophageal cancer, (ii) a decline of $9.2 million in spending due to discontinuance of development of PA-2794, (iii) a decline of $7.8 million due to a decline in expenses related to the development of new processes and the performance of test runs related to installed equipment of our existing manufacturing facilities to support the supply of BETAFERON® interferon beta-1b to Schering and (iv) a net decline of $5.2 million in spending related to the pre-registration activities of CUBICIN® (daptomycin) for treatment of complicated skin and soft tissue infections. During 2003 we recorded $10.6 million of expense associated with a fee paid under a license agreement with Cubist Pharmaceuticals, Inc. for the development and commercialization of Cubist s antibiotic daptomycin, as discussed below.

In 2004, we expensed $6.0 million to fund the remaining obligations of the SILCAAT trial due to our assessment of no future benefit from the trial.

In March 2004, we entered into a worldwide, exclusive, multi-product, collaborative arrangement with XOMA Ltd. for the development and commercialization of antibody products for the treatment of cancer. Under the terms of the arrangement, the parties agreed to jointly research, develop, and commercialize multiple antibody product candidates. Under the arrangement, the parties agreed to share development and commercialization expenses, including preclinical and clinical development, manufacturing and worldwide marketing costs, as well as revenues, generally on a 70-30 basis, with our share being 70% and XOMA s share being 30%. We agreed to make an initial payment of $10.0 million, which was paid as of December 31, 2004, and classified as prepaid research and development expense. The prepaid expense is being amortized on a straight-line basis over a five-year period of benefit. Amortized research and development expense of $1.5 million and $2.0 million were recorded for the years ended December 31, 2004 and 2005, respectively. We agreed to make a loan facility of up to $50.0 million available to XOMA, starting on January 1, 2005 to fund 75% of XOMA s share of development expenses. Under this arrangement, we made $12.1 million in loan advances to XOMA as of December 31, 2005. Interest payable by XOMA is due when the principal is due and is additive to the $50.0 million available principal. Interest payable of $0.3 million was added to the outstanding balance as of December 31, 2005. The loan advances were recorded at the estimated fair value based upon an interest rate for a similar loan facility from a bank to a similar counterparty. The recorded amount will be accreted to full face value over the life of the outstanding facility based on the effective interest method. At December 31, 2005, $7.1 million was recorded as Non-current notes receivable in the Consolidated Balance Sheet for these loan advances.

In October 2003, we entered into a license agreement with Cubist Pharmaceuticals, Inc. for the development and commercialization of Cubist s antibiotic CUBICIN® (daptomycin) in Western and Eastern Europe, Australia, New Zealand, India and certain Central American, South American and Middle Eastern countries. In exchange for these development and commercialization rights, we have agreed to pay Cubist up to $50.0 million. This $50.0 million includes $18.0 million, which was paid by us up front in the fourth quarter 2003, $10.0 million of which was used to purchase restricted Cubist common stock at a 50 percent premium over market price and up to $32.0 million of additional payments to Cubist upon the achievement of certain regulatory and sales milestones. We also agreed to pay Cubist a tiered royalty on CUBICIN® marketed by us. We recorded $10.6 million of the up front payment related to the purchase of in-process research and development, as research and development expense in 2003. In January 2006, European Commission granted marketing approval to us for CUBICIN®, a first-in-class IV antibiotic. The marketing approval was granted in the 25 member states of the European Union, Iceland, Liechtenstein and Norway. Under the approval, CUBICIN® is indicated for the treatment of complicated skin and soft-tissue infections (cSSTI) caused by Gram-positive bacteria. The CUBICIN® antibiotic is also approved by the FDA for the treatment of complicated skin and skin structure infections caused by Gram-positive bacteria, and is marketed in the United States by Cubist Pharmaceuticals, Inc. CUBICIN® antibiotic is manufactured for us by Cubist Pharmaceuticals, Inc.

In October 2003, we acquired all of Pfizer, Inc. s, formerly Pharmacia Corporation s, interest in tifacogin, in return for which Pfizer will receive royalties on future sales of tifacogin. In the second quarter 2004, we began enrolling patients in our Phase III trial for tifacogin as a treatment for patients with severe community-acquired pneumonia. In December 2005 an independent Data Monitoring Committee completed an interim analysis of clinical data from the study and recommended the continuation of the study.

In April 2003, we acquired exclusive worldwide development and commercial rights from Novartis for PULMINIQ (cyclosporine, USP) inhalation solution, a therapy under evaluation for treatment of rejection and reduction of mortality in lung transplant recipients for $0.5 million, which was expensed as research and development costs in 2003. In 2004, we submitted a new drug application to the FDA for marketing approval of PULMINIQ . On July 14, 2005, we received an action letter from the FDA stating that the company s New Drug Application (NDA) for PULMINIQ (cyclosporine, USP) inhalation

solution is approvable but, in light of the fact that the application was based on a single-center clinical trial with a small patient population, an additional pre-approval study would be required to confirm the efficacy of the drug.

In the fourth quarter of 2002, we reached an agreement in principle to transfer responsibility for the SILCAAT trial, a Phase III study for recombinant human interleukin-2 (IL-2, aldesleukin), to the National Institutes Allergy and Infectious Disease (NIAID) and the University of Minnesota. Responsibility for the SILCAAT study was transferred to NIAID and University of Minnesota effective February 14, 2003. Under the agreement, we funded $6.0 million and $12.0 million for the years ended December 31, 2003 and 2004, respectively. There are no remaining funding obligations due under this agreement.

Research and development expenses may fluctuate from period to period depending upon the stage of certain projects and the level of pre-clinical and clinical trial-related activities.

Selling, general and administrative expenses The increase in selling, general and administrative expenses in 2005 as compared with 2004 was primarily due to (i) $9.1 million for pre-launch costs for CUBICIN® (daptomycin), (ii) $1.1 million of pre-launch costs for PULMINIQ (cyclosporine, USP) inhalation solution and (iii) $0.6 million due to movement in the Euro to U.S. Dollar exchange rate. These increases were partially offset by $5.1 million decline for various marketing and promotional activities that have been discontinued.

The increase in selling, general and administrative expenses in 2004 as compared with 2003 was primarily due to (i) $ 5.5 million for increased expenses for new product support, (ii) $5.5 million for the Euro to U.S. Dollar exchange rate fluctuation, (iii) $4.5 million for increased expenses for programs and headcount in support of TOBI® tobramycin and international marketing, (iv) $4.2 million related to increased costs of our facilities, (v) $1.7 million increase for support to enhance business processes and (vi) $1.2 million for increased sales and medical affairs support.

Amortization expense Amortization expense was consistent in 2005, 2004 and 2003 and relates to the distribution rights acquired upon acquisition of Pulmopharm in the third quarter 2002 and intangible assets from our acquisition of PathoGenesis Corporation in 2000, which we accounted for under the purchase method of accounting and allocated a portion of the purchase price to purchased technologies, acquired intangible assets and goodwill.

Other

We view certain other revenues and expenses, particularly certain royalty and license fee revenues primarily related to HIV and HCV-related patents, and unallocated corporate expenses, as not belonging to any one reportable segment. Notably, revenues earned from diagnostic products are included in our other segment and revenues earned from blood screening are included in our Blood Testing segment. As a result, we have aggregated these items into an Other segment.

	Year Ended December 31,			$ Change		% Change	
	2005	2004	2003	2005 vs. 2004	2004 vs. 2003	2005 vs. 2004	2004 vs. 2003
	($ in 000 s, except percentages)						
Royalty and license fee revenues	$ 132,827	$ 123,608	$ 74,290	$ 9,219	$ 49,318	7.5 %	66.4 %
Selling, general and administrative expenses	$ 148,160	$ 116,933	$ 86,867	$ 31,227	$ 30,066	26.7 %	34.6 %
Purchased in-process research and development	$	$ 9,629	$ 45,300	$ (9,629)	$ (35,671)	(100)%	(78.7)%
Interest expense	$ 30,615	$ 26,093	$ 19,104	$ 4,522	$ 6,989	17.3 %	36.6 %
Interest and other income, net	$ 86,692	$ 56,797	$ 38,892	$ 29,895	$ 17,905	52.6 %	46.0 %

Royalty and license fee revenues Our other segment earns royalties on third party sales of, and license fees on, several products. The majority of royalty and license fee revenues related to the use of our HCV and HIV-related patents for diagnostic testing purposes by various third parties.

Roche settlement In October 2000, we entered into three license agreements with Roche and several of its affiliated companies related to the settlement of certain litigation in the U.S. and certain other countries for use of our HCV and HIV nucleic acid testing intellectual property. Two agreements relate to *in vitro* diagnostics products. The third agreement relates to blood screening. See Blood Testing Royalty and license fee revenues above for more information on the blood screening agreement.

Under the hepatitis C virus agreement, we received $85.0 million, of which we recognized $40.0 million in the fourth quarter 2000. We deferred the remaining $45.0 million, which became non-refundable through 2005. During 2003, 2004 and 2005, we recognized $8.4 million, $11.0 million and $13.9 million, respectively. The agreement also provides for royalties on future sales related to Roche s use of our HCV-related patent in its *in vitro* diagnostic products. Royalty revenue increased in 2005 as compared with 2004, by $7.1 million or 13.8%. Royalty revenues increased in 2004 as compared with 2003, by $4.4 million or 9.5%.

The HIV agreement with Roche provides for royalties on sales related to Roche s use of our HIV-related patent in its *in vitro* diagnostic products. Royalty revenues recognized under this agreement decreased by $12.6 million in 2005 as compared with 2004 and increased by $40.0 million in 2004 as compared with 2003. The decrease in 2005 as compared with 2004 was mainly due to the recognition of $35.6 million in 2004 of deferred royalties and license fees and a nonrefundable portion of a royalty payment from the September 10, 2004 settlement. This was partially offset by royalties of $26.5 million in 2005 from the September 10, 2004 settlement. The increase in 2004 as compared with 2003 was mainly due to the recognition of $35.6 million in 2004 of deferred royalties and license fees and a nonrefundable portion of a royalty payment from the September 10, 2004 settlement. The September 10, 2004 settlement agreement with Roche is described in more detail below.

An HIV-related patent directed to nucleic acid testing methods for HIV-1 was issued in the U.S. on March 13, 2003. This patent will expire seventeen years from the date of issuance. The issuance of the patent triggered a milestone payment to us of $10.0 million from Roche, which was received in April 2003. As permitted under the terms of its licensing agreement, Roche decided to institute arbitration proceedings in regard to the application of the U.S. patent. We had deferred recognition of the $10.0 million milestone payment, interest, royalties received and royalties accrued under the patent until the resolution of this dispute. On September 10, 2004, we reached a settlement agreement with Roche. Under the terms of the settlement agreement, the milestone payment along with any royalties received prior to March 31, 2004 became non-refundable. Accordingly, in 2004, we recognized $10.0 million in license fees and $21.8 million in royalties up until June 30, 2004, which had previously been deferred, of which $16.3 million has been recognized as revenue in our other segment and $5.5 million has been recognized as revenue in our Blood Testing segment. We also recognized $0.8 million in interest on the license fee. Also under the settlement agreement, in 2005, we received a lump-sum payment of $78.0 million in lieu of royalties beyond January 1, 2005. Roche may elect under the terms of the agreement to obtain a partial refund and revert to paying royalties on the sales of its products in North America. The amount of such potential refund ranges between $64.0 million and $0.0 million. The amount of the refund available to Roche decreases in increments over the quarters of 2005 and 2006. As such, we are recognizing $64.0 million of the $78.0 million payment as revenue during 2005 and 2006. The remaining $14.0 million is non-refundable and was recognized as revenue in 2004, of which $9.3 million has been recognized as revenue in our other segment and $4.7 million has been recognized as revenue in our Blood Testing segment. Currently, the applicable issued HCV-related patents expire in 2015 for the U.S. and 2010 in Europe. The applicable issued HIV-related patent in Europe expired in October 2005.

For 2005, we recognized an aggregate of $40.0 million, with $26.5 million of revenue from this settlement recognized in our other segment and $13.5 million of revenue from this settlement recognized in our Blood Testing segment. We expect to recognize the remaining $24.0 million during 2006.

The impact on revenues in 2005 and 2004 from these items from the September 10, 2004 settlement with Roche is summarized below.

	2005 Other Segment (In thousands)	Blood Testing Segment	Total	2004 Other Segment (In thousands)	Blood Testing Segment	Total
Deferred revenues recognized	$	$	$	$ 16,313	$ 5,453	$ 21,766
Deferred license fee recognized				10,000		10,000
Non-refundable portion of Roche settlement	26,500	13,500	40,000	9,333	4,667	14,000
Total royalty and license fee revenue	$ 26,500	$ 13,500	$ 40,000	$ 35,646	$ 10,120	$ 45,766

Roche PCR agreement Under a July 1991 agreement between Roche Limited and Cetus Corporation (a company acquired by Chiron), we received royalties on sales of polymerase chain reaction products and services sold by Roche and its licensees. In 2004, we recognized a $3.0 million settlement with Roche regarding this agreement. We did not recognize any revenue under this agreement in 2005 and 2003.

Bayer A cross-license agreement provides for royalties to us on HIV and hepatitis C virus products sold by Bayer Corporation. Royalties increased $1.9 million in 2005 compared with 2004 due to increased product sales by Bayer. Royalties were consistent in 2004 as compared with 2003.

Centocor In 2005, we recognized $11.3 million of upfront payments and royalties from a settlement with Centocor relating to certain patents.

The balance of royalty and license fee revenues consisted of various other agreements, which individually were not material.

Royalty and license fee revenues may fluctuate based on the nature of the related agreements, the timing of receipt of license fees and the expiration of patents. Results in any one period are not necessarily indicative of results to be achieved in the future. In addition, our ability to generate additional royalty and license fee revenues may depend, in part, on our ability to market and capitalize on our technologies.

Selling, general and administrative expenses The increase in selling, general and administrative expenses in 2005 as compared with 2004 was primarily due to (i) $9.7 million of costs associated with the proposed merger between Chiron and Novartis AG, (ii) $8.7 million for higher employee related expenses, (iii) $5.9 million for higher costs related to compliance with the Sarbanes-Oxley Act, (iv) $4.5 million of additional legal costs associated with the FLUVIRIN® vaccine-related developments discussed above under *Influenza Virus Vaccines Recent Events,* and (v) $4.1 million in legal costs related to the defense of our patents and technology. These increases were partially offset by lower facility costs of $7.1 million.

The increase in selling, general and administrative expenses in 2004 as compared with 2003 was primarily due to $12.1 million in legal costs related to the FLUVIRIN® vaccine developments discussed above under *Influenza Virus Vaccines Recent Events,* $12.9 million in legal costs related to the defense of our patents and technology and $5.4 million from costs related to compliance with the Sarbanes-Oxley Act. These increases were partially offset by the effect of a $4.0 million donation to Chiron Foundation in 2003 and $1.2 million of lower employee related expenses.

Purchased in-process research and development Purchased in-process research and development charged to operations was $9.6 million and $45.3 million in 2004 and 2003, respectively. There was no such charge in 2005.

On July 2, 2004, we acquired Sagres Discovery and accounted for the acquisition as an asset purchase. We allocated the purchase price based on fair value of the assets acquired and liabilities assumed. We allocated $9.6 million of the purchase price to purchased in-process research and development, which we charged to operations in the third quarter 2004. We did not anticipate that there would be any alternative future use for the purchased in-process research and development.

On July 8, 2003, we acquired PowderJect and accounted for the acquisition as a business combination. We allocated the purchase price based on the fair value of the assets acquired and liabilities assumed. We allocated $45.3 million of the purchase price to purchased in-process research and development, which we charged to operations in 2003. We did not anticipate that there would be any alternative future use for the in-process research and development. In valuing the purchased in-process research and development, we used probability-of-success-adjusted cash flows and a 14% discount rate. Cash flows from projects including those relating to (i) certain travel vaccines and (ii) vaccines for allergies were assumed to commence between 2004 and 2012.

Interest expense The increase in interest expense in 2005 as compared with 2004 primarily related to the effect of twelve months versus six months of interest expense recognized on the $385.0 million convertible debentures that were issued on June 22, 2004, partially offset by the lower interest expense recognized on the Liquid Yield Option Notes (LYONs), the majority of which were put to us by the debt holders in June 2004. The $385.0 million convertible debentures incur interest at a higher rate than the LYONs.

The increase in interest expense in 2004 as compared with 2003 primarily related to the effect of twelve months versus five months of interest expense recognized on the $500.0 million convertible debentures that we issued on July 30, 2003. Also, interest expense increased due to interest on the $385.0 million convertible debentures that we issued on June 22, 2004. These increases were partially offset by lower interest expense from certain of our Liquid Yield Options Notes (LYONs), which were put to us by the debt holders on June 12, 2004.

Interest and other income, net Interest and other income, net, primarily consisted of interest income on our cash and investment balances and other non-operating gains and losses. We recognized interest income of $37.0 million, $23.4 million and $23.2 million in 2005, 2004 and 2003, respectively.

The increase in interest income in 2005 as compared with 2004 primarily was due to higher average cash and investment balances and higher average interest rates.

In 2005, 2004 and 2003, we recognized gains of $44.3 million, $34.3 million and $9.4 million, respectively, related to the sale of certain equity securities. The increases in both 2005 and 2004 are primarily due to the termination of certain equity forward contracts and the related sale of underlying securities.

In 2005 and 2004, we recognized losses attributable to the impairment of equity securities of $1.3 million and $1.4 million, respectively. There were no losses attributable to impairment of equity securities in 2003.

In 2005, we recognized a $6.0 million settlement regarding a dispute with one of our competitors regarding certain Chiron patents.

In 2005, we recognized a $2.6 million insurance settlement regarding a building fire at our Emeryville campus.

On December 31, 1998, we completed the sale of our 30% interest in General Injectibles & Vaccines, Inc., a distribution business, to Henry Schein, Inc. and received payment in full of certain advances we made to General Injectibles & Vaccines. The agreement also provided for us to receive additional payments, calculated as a pre-determined percentage of Henry Schein s gross profit, through 2003. We received $4.2 million and $2.0 million for 2003 and 2002 in 2004 and 2003, respectively.

Income taxes The effective tax rate for 2005 was 11.0% of pretax income from continuing operations. The effective tax rate for 2004 was 28.2% of pretax income from continuing operations, including the charge for purchased in process research and development related to the Sagres acquisition, which was not tax deductible, and 25.0% of pre-tax income excluding such charge. The effective tax rate was higher in 2004 principally due to the impact of inter-company transfers of certain product rights in 2004, which increased foreign income taxes. There were no such transfers of product rights in 2005. Further, the effective tax rate in 2005 also includes increased benefits from state tax credits and certain foreign tax benefits which are, as a percentage of pre-tax income, higher than would be the case with higher levels of pre-tax income from FLUVIRIN® influenza vaccine sales. We do not consider this tax rate to be indicative of our effective tax rate going forward. The effective tax rate may be affected in future periods by changes in management s estimates with respect to our deferred tax assets and other items affecting the overall tax rate.

Discontinued operations In a strategic effort to focus on our core businesses of Blood Testing, vaccines and biopharmaceuticals, we completed the sale of Chiron Diagnostics and Chiron Vision in 1998 and 1997, respectively.

There was no gain (loss) from discontinued operations, net of taxes in 2005.

Chiron and Bayer Corporation, or Bayer, were involved in a dispute with respect to their respective rights to certain royalty refunds receivable for which a settlement was reached in 2004. Under this settlement agreement, we made a settlement payment to Bayer in 2004. This settlement includes an agreement that all outstanding items with Bayer related to the sale of Chiron Diagnostics are resolved and no future indemnity obligations are required. We released previously established reserves deemed to be excess following this settlement. This settlement resulted in a net gain of $12.4 million in 2004. This net gain primarily relates to a tax benefit as a result of the settlement payment to Bayer. In 2004, Chiron and the IRS entered into a settlement agreement closing the open tax years 1996 to 1998. Pursuant to this settlement agreement, we recognized a tax benefit of approximately $12.5 million in 2004.

We reversed approximately $2.3 million related to unutilized reserves for Chiron Diagnostics and Chiron Vision in 2003. In 2003, Chiron and Bayer reached a settlement agreement relating to certain claims raised by Bayer under the Stock Purchase Agreement dated September 17, 1998, between Chiron and Bayer for Chiron Diagnostics. Under this settlement agreement, we made a payment to Bayer in 2003. Pursuant to this settlement, we recorded a charge, net of adjustment to our previously provided reserve for indemnity obligations of $7.6 million, offset by an income tax benefit of $9.0 million, resulting in a net gain of $1.4 million in 2003. We recognized an aggregate income tax benefit of $12.2 million in 2003 of which $9.0 million related to the settlement agreement between Bayer and $3.2 million related to the reversal of valuation allowances against deferred taxes that were established at the time of the sale of Chiron Diagnostics.

New Accounting Standards In December 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment* (SFAS 123(R)), which requires the cost resulting from all share-based payment transactions to be recognized in the consolidated financial statements. That cost will be measured based on the fair value of the equity instruments issued or on the fair value of liabilities incurred. Under SFAS 123(R), the fair-value-based method for recognition or disclosure of compensation expense will be applied using the modified prospective application transition method or the modified retrospective application transition method. We

currently measure compensation expense for our stock-based employee compensation under the intrinsic method. Current option values determined using the Black-Scholes-Merton formula, used for purposes of proforma disclosure, may not be indicative of results from the valuation methodologies we finally adopt. The effective date of SFAS 123(R) is the first reporting period beginning after June 15, 2005. However, on April 14, 2005, the Securities and Exchange Commission (SEC) announced the adoption of a new rule that delays the effective date of SFAS 123(R) for registrants, such as Chiron, that are not small business issuers. The SEC s new rule allows calendar year non-small business issuers to implement SFAS 123(R) at the beginning of 2006, which makes SFAS 123(R) effective for Chiron in the first quarter of 2006.

We are currently evaluating the transition methods, option valuation methodologies and assumptions in light of SFAS 123(R) and, therefore, cannot estimate the impact of our adoption at this time, although we expect that our adoption will have a material impact on our consolidated financial statements.

On October 22, 2004, the American Jobs Creation Act of 2004 (the Act) was signed into law. The Act includes a temporary incentive for U.S. multinationals to repatriate accumulated income earned outside the U.S. at an effective tax rate of 5.25%. Through December 31, 2005, we have not provided deferred taxes on foreign earnings because such earnings are intended to be indefinitely reinvested outside the U.S. We did not repatriate any accumulated earnings from outside the U.S. in either 2004 or 2005.

Liquidity and Capital Resources

Our capital requirements have generally been funded by cash flow from operations, borrowings from commercial banks and issuance of convertible debt securities and common stock. Our cash, cash equivalents and investments in marketable debt securities, which totaled $1,408.8 million at December 31, 2005, are invested in a diversified portfolio of fixed income securities, including money market instruments, corporate notes and bonds, and government agency securities issued by financial institutions and other issuers with strong credit ratings. By policy, the amount of credit exposure to any one institution is limited. Investments are generally not collateralized and primarily mature within three years.

In December 2005, we received net proceeds of $300.0 million, following the sale of 6,896,552 newly issued shares of our common stock at a price of $43.50 per share to a subsidiary of Novartis. Under provisions of the 1994 Subscription Agreement with Novartis, as amended, Chiron exercised its right on October 30, 2005, to have Novartis purchase the shares.

The recent events regarding FLUVIRIN® vaccine, as discussed above under Management s Discussion and Analysis of Financial Condition and Results of Operations *Influenza Virus Vaccines Recent Events,* will continue to impact our cash flow going forward. As we continue to implement our remediation plan, our efforts will entail additional cash payments, which will be material. The MHRA s lifting of our license suspension is conditioned upon the understanding that our commitment to remediation will continue.

In addition, we have incurred and expect to continue to incur substantial expense relating to the shareholder class action and derivative private lawsuits and other claims arising out of or related to these developments regarding FLUVIRIN® vaccine. The results of any such investigations, proceedings or disputes could have a material adverse effect on our cash flow.

Our previous inability to supply FLUVIRIN® vaccine has led to loss of market share and may lead to loss of additional market share in future seasons. Following the announcement of our FLUVIRIN® license suspension, competitors announced plans to introduce influenza vaccine products in the United States and sought expedited regulatory approval to do so. Even though the license suspension has been lifted, and we returned to the U.S. market for the 2005-2006 influenza season, some of our customers may continue to choose to purchase influenza vaccine from other providers as their products become available in the

United States. Delays in start-up procedures for ramping up to full production and normal manufacturing issues inherent in the complexity of influenza vaccine production, have adversely affected the amount of FLUVIRIN® vaccine that we are able to produce for the 2005-2006 influenza season and may result in further loss of market share. Loss of market share could have a material adverse effect on cash flow.

The recent events regarding BEGRIVAC vaccine, as discussed above under Management s Discussion and Analysis of Financial Condition and Results of Operations *Influenza Virus Vaccines Recent Events,* may impact our cash flow going forward. We were unable to supply any BEGRIVAC vaccine doses for the 2005-2006 influenza season, which eliminated any cash flows we would have received from the sale of BEGRIVAC vaccine. Our inability to supply BEGRIVAC vaccine as planned to non-U.S. markets may also lead to loss of market share in future seasons. Loss of market share could have a material adverse effect on cash flow. In addition, while we are in the process of implementing remedial measures to address the product sterility issue, including facility modifications, our remediation efforts will entail cash payments for additional capital and other expenditures, which could be material. If we are unable to return BEGRIVAC influenza vaccine to the market, it could have a material adverse effect on our cash flow.

In addition, certain distributors and other parties with whom we had contracted to supply influenza vaccine may make claims against us as a result of Chiron not supplying influenza vaccine. Any such claims may cause us to incur substantial expense and require significant time and attention from our management. The results of any such claims could have a material adverse effect on our cash flow.

For additional information concerning the risks we face as a result of these influenza vaccine developments, see Factors That May Affect Future Results *Developments with respect to influenza vaccines over the past year may harm our business and results of operations*. For additional information on the private lawsuits and other claims, see Part I, Item 3. Legal Proceedings of this Report on Form 10-K.

On June 12, 2004, certain holders of our Liquid Yield Option Notes (LYONs), at their option, tendered LYONs with $649.9 million in aggregate principal amount at maturity, which we were required to purchase. The purchase price for the tendered LYONs was $584.31 in cash per $1,000 in principal amount at maturity. The aggregate purchase price for all the LYONs validly surrendered for purchase was $379.7 million. At December 31, 2005, there remains $80.1 million outstanding in aggregate principal amount at maturity with a current accreted balance of $48.3 million. At the option of the holders, we may be required to purchase all, or a portion, of the remaining LYONs on June 12, 2006 at $608.04 for each note with face value of $1,000. If the holders require us to purchase all, or a portion, of the LYONs, we may choose to pay the purchase price in cash, Chiron common shares, or any combination of the two. Our intent is to settle the purchase price in cash. Accordingly, $48.3 million is included in the current portion of long-term debt in the Consolidated Balance Sheet at December 31, 2005.

On June 22, 2004, we issued $385.0 million aggregate principal amount of new convertible debentures, which mature on June 30, 2034. The convertible debentures accrue interest at a rate of 2.75% per year with interest payable each June 30 and December 30 commencing December 30, 2004. The debentures are senior, unsecured obligations and rank equal in right of payment with all of our existing and future unsecured and unsubordinated indebtedness.

Under the terms of the Investment Agreement, Novartis agreed to guarantee certain of our obligations under revolving credit facilities through January 1, 2008, the date on which the guarantee will expire. The principal amount of indebtedness under the guaranteed credit facilities outstanding at any one time may not exceed a specified cap. That cap was $402.5 million. In November 1996, we and Novartis agreed that we could increase the maximum borrowing amount under the guaranteed credit facilities by up to $300.0 million, for a maximum borrowing amount under the cap of $702.5 million. In exchange for this increase, the amount of our common stock required to be purchased by a Novartis affiliate, at our request,

under the Subscription Agreement, would be reduced by an equal amount. The maximum amount Novartis is required to guarantee pursuant to the terms of the Investment Agreement has been reduced by $109.8 million following an election by us in December 2005, to exercise our subscription rights under the Investment Agreement, decreasing the cap to $592.7 million. Through February 2006, Novartis guaranteed a $100.0 million U.S. credit facility for our benefit for which there were no borrowings outstanding at December 31, 2005 and $173.3 million of our capital lease commitments. The U.S. credit facility has since expired and at our election was not renewed and is thus no longer guaranteed by Novartis. As a result of these guarantees and the conversion of $9.8 million of bonds in 2000 into shares of our common stock, there remains approximately $417.7 million of the guarantee available following the exercise of our subscription rights and our subsequent election to increase the amount Novartis may be required to guarantee to the maximum borrowing amount.

We believe that our cash, cash equivalents and marketable debt securities, together with funds provided by operations and borrowing and leasing arrangements, will be sufficient to meet our foreseeable operating cash requirements over at least the next twelve months including cash utilized for our stock repurchase program and our contractual obligations of $402.9 million in the next twelve months as discussed in the contractual obligation table below. We also believe that our cash, cash equivalents and marketable debt securities, together with funds provided by operations and lease arrangements, will be sufficient to meet our contractual obligations of $1.5 billion arising after twelve months as discussed in the Contractual Obligations table below. In addition, we believe we could access additional funds from the debt and capital markets should the need arise. As noted above, if we are unable to maintain FLUVIRIN® vaccine in the market and return BEGRIVAC influenza vaccine to the market, whether through loss of regulatory approvals, market share or otherwise, it would have a material adverse effect on our cash flow.

Sources and Uses of Cash

We had cash and cash equivalents of $291.4 million and $209.5 million at December 31, 2005 and 2004, respectively.

Operating activities In 2005, net cash provided by operating activities was $249.2 million as compared with $170.7 million in 2004. The increase in cash provided by operating activities was primarily due to higher income from continuing operations before depreciation, amortization and other non-cash charges, mainly due to higher FLUVIRIN® vaccine sales of $96.5 million (compared to FLUVIRIN® vaccine sales of $2.3 million in 2004 from the 2003-2004 influenza season), following the lifting of our license suspension to manufacture FLUVIRIN® influenza virus vaccine in our Liverpool facility. This subsequently allowed us to resume shipment of the product for the 2005-2006 influenza season. Cash provided by operating activities also increased due to (i) a $78.0 million lump-sum payment received in lieu of royalties beyond January 1, 2005 as part of the Roche settlement reached on September 10, 2004, (ii) increased sales of our travel vaccines, PROCLEIX® product sales and TOBI® tobramycin, partially offset by decreases in sales of our pediatric and other vaccines and (iii) an increase in other current liabilities at December 31, 2005 as compared with December 31, 2004. These increases were partially offset by (i) costs associated with our remediation efforts for our Liverpool plant and legal costs related to the FLUVIRIN® vaccine developments, (ii) the lost contribution of sales of BEGRIVAC (there were no sales of BEGRIVAC vaccine in 2005 compared to sales of $52.7 million in 2004), (iii) increased selling, general and administrative expenses in 2005 primarily due to Novartis transaction-related costs, the pre-launch program for CUBICIN® daptomycin in Europe, higher employee-related costs, compliance with the Sarbanes-Oxley Act and higher FLUVIRIN® vaccine-related legal costs, (iv) a larger increase in accounts receivable at December 31, 2005 as compared with the increase in accounts receivable at December 31, 2004, and (v) a smaller increase in accounts payable, accrued expenses and income taxes payable at December 31, 2005 as compared with December 31, 2004.

In 2004, net cash provided by operating activities was $170.7 million as compared with $413.9 million in 2003. The decrease in cash provided by operating activities was primarily due to lower income from continuing operations before depreciation, amortization and other non-cash charges, which decreased mainly due to the suspension of our license to manufacture FLUVIRIN® influenza virus vaccine in our Liverpool facility which prevented the release of any of the product during the 2004-2005 influenza season. Cash provided by operating activities also decreased due to (i) increased selling, general and administration expenses in 2004 primarily due to the movement of the Euro and British Pound exchange rates, twelve months of selling, general and administrative expenses from PowderJect in 2004 compared to approximately six months in 2003 and increased legal costs, (ii) lower royalty payments of BETASERON® and BETAFERON® interferon beta-1b due to a decline in the royalty rate by five percentage points pursuant to our contractual arrangement with Schering, and lower royalty payments received under the Roche royalty arrangements in 2004 compared with 2003 and (iii) $14.4 million of cash received as a result of the Biogen and Serono settlements in connection with the McCormick patents in 2003. These decreases were offset by (i) lower tax payments in 2004 as compared with 2003, (ii) a payment to Bayer Corporation in 2003 from a settlement agreement relating to certain claims raised by Bayer in connection with the Stock Purchase Agreement dated September 17, 1998 and (iii) increased product sales of PROCLEIX® assays and TOBI® tobramycin in 2004.

Investing activities In 2005, net cash used in investing activities consisted of purchases of investments in marketable debt securities of $1,163.2 million, capital expenditures of $200.0 million, issuance of notes receivable of $12.1 million, purchases of equity securities and interests in affiliated companies of $4.9 million, cash paid for acquisitions net of cash acquired of $4.8 million, and other uses of cash of $13.3 million. Included in net cash paid for acquisitions was $4.0 million for previously accrued costs in connection with acquisition costs related to the acquisition of PowderJect and $0.8 million of cash paid for the acquisition of Sagres. Cash used in investing activities was offset by proceeds from maturities of investments in marketable debt securities of $610.5 million, proceeds from sales of investments in marketable debt securities of $226.5 million, proceeds from the sale of equity securities and interests in affiliated companies of $36.9 million and proceeds from the sale of assets of $0.2 million.

In 2003, our Board of Directors approved $50.7 million in expenditures for a 25-year building lease and $42.2 million for capital improvements, both of which are part of a $97.0 million project for expansion and replacement of our influenza vaccines primary manufacturing facility in Liverpool, United Kingdom. The new manufacturing facility will replace a portion of the existing influenza vaccines manufacturing facilities in Liverpool, United Kingdom and is anticipated to be available in 2009 for the manufacture of influenza vaccines, subject to regulatory approval. In December 2003, we entered into a 25-year lease for the building. As of December 31, 2005, we have incurred $23.0 million for the capital improvements portion of the project.

The purchases of equity securities and interests in affiliated companies in 2005 consisted of equity contributions under several venture capital funds including a $1.6 million capital contribution under two 2003 limited partnership agreements, a $0.6 million capital contribution under a 2002 limited partnership agreement, a $2.1 million capital contribution under a 2001 limited partnership agreement and a $0.6 million capital contribution under a 2000 limited partnership agreement.

In 2003, we became a limited partner of Burrill Life Sciences Capital Fund, L.P. We agreed to pay $10.0 million over six years, of which $4.7 million has been paid through December 31, 2005 for a 5.14% ownership. In 2003, we became a limited partner of Forward Venture V, L.P. We agreed to pay $5.0 million over five years, of which $0.6 million has been paid through December 31, 2005, for a 3.45% ownership. In 2002, we became a limited partner of TPG Biotechnology Partners, L.P. We agreed to pay $5.0 million over ten years, of which $2.8 million has been paid through December 31, 2005, for a 2.83% ownership. In 2001, we became a limited partner of Forward Venture IV, L.P. We agreed to pay

$15.0 million over ten years, of which $13.1 million has been paid through December 31, 2005, for a 6.35% ownership. In 2000, we became a limited partner of Burrill Biotechnology Capital Fund, L.P. We agreed to pay $25.0 million over five years, of which $21.7 million has been paid through December 31, 2005, for a 23.26% ownership.

In 2004, net cash used in investing activities consisted of purchases of investments in marketable debt securities of $796.9 million, capital expenditures of $183.7 million, cash paid for acquisitions net of cash acquired of $34.9 million, other uses of cash of $10.7 million and purchases of equity securities and interests in affiliated companies of $6.6 million. Included in net cash paid for acquisitions was $8.2 million for previously accrued costs in connection with the acquisition of PowderJect, $15.5 million of cash delivered on the divestiture of certain operations in Wisconsin, the U.K., and Sweden and $11.2 million of cash paid for the acquisition of Sagres. Cash used in investing activities was offset by proceeds from sales of investments in marketable debt securities of $431.1 million, proceeds from maturities of investments in marketable debt securities of $286.5 million, proceeds from the sale of equity securities and interests in affiliated companies of $38.7 million, proceeds from the sale of assets of $3.0 million and proceeds from notes receivable of $1.5 million.

The purchases of equity securities and interests in affiliated companies in 2004 consisted of equity contributions under several venture capital funds including a $2.6 million capital contribution under two 2003 limited partnership agreements, a $0.3 million capital contribution under a 2002 limited partnership agreement, a $2.0 million capital contribution under a 2001 limited partnership agreement and a $1.4 million capital contribution under a 2000 limited partnership agreement. In addition, we contributed $0.3 million to our 51%-owned joint venture Indian subsidiary in 2004.

In 2003, net cash used in investing activities consisted of purchases of investments in marketable debt securities of $920.8 million, cash paid for acquisitions, net of cash acquired of $815.4 million, capital expenditures of $139.4 million, purchases of equity securities and interests in affiliated companies of $14.2 million and other uses of cash of $0.9 million. In 2003, cash paid for acquisitions, net of cash acquired, consisted of cash paid to acquire PowderJect, net of cash acquired, of $814.7 million and cash paid for acquisition costs related to the acquisitions of PathoGenesis Corporation and Matrix Pharmaceutical of $0.7 million. Cash used in investing activities was offset by proceeds from sales of investments in marketable debt securities of $793.2 million, proceeds from maturities of investments in marketable debt securities of $420.5 million, proceeds from the sale of equity securities and interests in affiliated companies of $12.6 million and proceeds from notes receivable of $0.8 million.

On July 8, 2003, we acquired PowderJect, a company based in Oxford, United Kingdom that develops and commercializes vaccines. We acquired all of the outstanding shares of common stock of PowderJect for a total purchase price of approximately $938.6 million. As part of the acquisition of PowderJect, we assumed the debt of PowderJect including convertible notes with a face value of 35.0 million British pounds (fair value of $57.0 million at July 8, 2003). We repaid the convertible notes during the third quarter 2003 and the payment is included in Repayment of debt and capital leases in the Consolidated Statement of Cash Flows for the year ended December 31, 2003.

The purchases of equity securities and interests in affiliated companies in 2003 consisted of (i) a payment of $6.7 million for the purchase of restricted Cubist common stock, (ii) a payment of $1.0 million for an equity investment in ZymeQuest and (iii) equity contributions under several venture capital funds including a $1.3 million capital contribution under two 2003 limited partnership agreements, a $0.6 million capital contribution under a 2002 limited partnership agreement, a $2.0 million capital contribution under a 2001 limited partnership agreement and a $2.7 million capital contribution under a 2000 limited partnership agreement.

Financing activities In 2005, net cash provided by financing activities consisted of $300.0 million of proceeds from the issuance of common stock (discussed below), $72.9 million of proceeds from the re-

issuance of treasury stock and $1.7 million of borrowings from a government agency. Cash provided by financing activities was partially offset by $1.0 million for the repayment of debt and capital leases.

On October 30, 2005, we exercised our right to have Novartis purchase newly issued shares of our common stock under provisions of our 1994 Subscription Agreement with Novartis, as amended. On December 8, 2005, we announced that we had sold 6,896,552 newly issued shares of our common stock at a price of $43.50 per share to a subsidiary of Novartis, for $300.0 million in the aggregate, following receipt of necessary regulatory approvals.

In 2004, net cash used in financing activities consisted of $383.0 million for the repayment of debt and capital leases, $135.0 million for the acquisition of treasury stock and $8.4 million for the payment of debt issuance costs. Cash used in financing activities was offset by $385.0 million of proceeds from issuance of convertible debentures due 2034 (discussed above), $69.1 million of proceeds from the reissuance of treasury stock and $5.6 million of borrowings from a government agency.

In 2003, net cash provided by financing activities consisted of $500.0 million of proceeds from the issuance of convertible debentures due 2033 (discussed below), $123.6 million of proceeds from the reissuance of treasury stock (related to stock option exercises), $2.1 million of proceeds from put options sold to reduce the costs of our share repurchase program, and $1.2 million from borrowings from a government agency in Italy. Cash provided by financing activities was offset by $207.7 million for the acquisition of treasury stock, $62.5 million for the repayment of debt and capital leases, $10.7 million for the payment of issuance costs on the convertible debentures and $2.4 million for the net repayment of short-term borrowings.

On July 30, 2003, we issued $500.0 million aggregate principal amount of convertible debentures, which mature on August 1, 2033. The debentures accrue interest at a rate of 1.625% per year. Interest is payable on February 1 and August 1 each year, commencing February 1, 2004. The debentures are senior, unsecured obligations of Chiron and rank equal in right of payment with all of our existing and future unsecured and unsubordinated indebtedness.

Our Board of Directors has, in the past, authorized the repurchase of our common stock on the open market. On December 5, 2003, the Board of Directors authorized Chiron to repurchase 5.0 million shares of Chiron common stock through December 31, 2004. Through December 31, 2004, we made purchases of 2.9 million shares at a cost of $126.5 million and the authorization to purchase the remaining 2.1 million shares expired unutilized. On March 10, 2005, the Board of Directors authorized Chiron to repurchase 5.0 million shares of Chiron common stock through December 31, 2005. There were no share repurchases in 2005.

In March 2004, we entered into a worldwide, exclusive, multi-product, collaborative arrangement with XOMA Ltd. for the development and commercialization of antibody products for the treatment of cancer. Under the terms of the arrangement, the parties agreed to jointly research, develop, and commercialize multiple antibody product candidates. Under the arrangement, the parties agreed to share development and commercialization expenses, including preclinical and clinical development, manufacturing and worldwide marketing costs, as well as revenues, generally on a 70-30 basis, with our share being 70% and XOMA s share being 30%. We agreed to make an initial payment of $10.0 million, which was paid as of December 31, 2004, and to make a loan facility of up to $50.0 million available to XOMA, starting on January 1, 2005 to fund 75% of XOMA s share of development expenses. Under this arrangement, we made $12.1 million in loan advances to XOMA as of December 31, 2005.

From time to time, we evaluate a number of business development opportunities. To the extent that we are successful in reaching agreements with third parties, these transactions may involve selling a significant portion of our current investment portfolio, incurring additional debt or issuing additional Chiron shares.

Contractual Obligations

Our contractual obligations as of December 31, 2005 were as follows:

	Obligations by period				
Contractual Obligations	**Total (in thousands)**	**Less than 1 year**	**1-3 years**	**3-5 years**	**More than 5 years**
Long-term debt (includes current portion)(1)	$ 940,292	$ 49,347	$ 2,284	$ 2,155	$ 886,506
Capital lease obligations(2)	165,794	2,624	5,248	157,922	
Other non-current liabilities(3)	112,828		18,364	6,648	87,816
Operating leases(4)	200,816	32,191	51,151	36,311	81,163
Purchase obligations:					
Technology services agreement(5)	39,600	9,600	19,200	10,800	
Purchase orders(6)	74,200	74,200			
Supply agreement(7)	128,100	18,300	36,600	36,600	36,600
Plant expansion(8)	19,200	4,800	9,600	4,800	
Berna biotech(9)	800	800			
Capital commitments(10)	43,868	41,299	2,569		
Infonet(11)	2,100	1,200	900		
Letters of credit(12)	14,825	14,825			
Research and development arrangements(13)	60,800	50,200	10,600		
Insurance-related items(14)	21,269	21,269			
Manufacturing and supply agreement(15)	17,500	12,000	5,500		
Supply agreement(16)	11,900	5,950	5,950		
Burrill Life Sciences Capital Fund, L.P.(17)	5,300	5,300			
Forward Venture V L.P(18)	4,400	4,400			
TPG Biotechnology Partners, L.P(19)	2,200	2,200			
Forward Ventures IV L.P(20)	1,900	1,900			
Burrill Biotechnology Capital Fund L.P(21)	3,300	3,300			
Contract manufacturing agreement(22)	20,488	6,308	7,880	6,300	
Revolving credit agreement(23)	2,500	2,500			
Loan facility(24)	37,900	37,900			
Managed services agreement(25)	467	467			
Total	$ 1,932,347	$ 402,880	$ 175,846	$ 261,536	$ 1,092,085

(1) On June 22, 2004, we issued $385.0 million aggregate principal amount of convertible debentures, which mature on June 30, 2034 (2034 Debentures). The convertible debentures accrue interest at a rate of 2.75% per year and interest is payable on each June 30 and December 30 commencing on December 30, 2004. The debentures are senior, unsecured obligations of Chiron and rank equal in right of payment with all of our existing and future unsecured and unsubordinated indebtedness.

The holders of the 2034 Debentures may require us to repurchase for cash all or part of the debentures on June 30, 2010, June 30, 2014, June 30, 2019, June 30, 2024 and June 30, 2029. The repurchase price will be equal to 100% of the principal amount of the debentures to be repurchased, plus accrued and unpaid interest, if any, up to the repurchase date.

On July 30, 2003, we issued $500.0 million aggregate principal amount of convertible debentures, which mature on August 1, 2033 (2033 Debentures). The convertible debentures accrue interest at a rate of 1.625% per year and interest is payable on February 1 and August 1 commencing February 1, 2004. The debentures are senior, unsecured obligations of Chiron and rank equal in right of payment with all of our existing and future unsecured and unsubordinated indebtedness.

The holders of the 2033 Debentures may require us to repurchase the debentures on August 1, 2008, August 1, 2013, August 1, 2018, August 1, 2023 and August 1, 2028. The repurchase price will be equal to the principal and accrued and unpaid interest. Payments for repurchases shall be made in the form of cash.

In June 2001, we issued zero coupon Liquid Yield Option Notes (LYONs) with a face value of $730.0 million and a yield to maturity of 2.0%. The LYONs were carried net of an original issue discount of $328.2 million, which was being accreted to interest expense over the life of the LYONs using the effective interest method. On June 12, 2004, certain LYONs holders, at their option, tendered $649.9 million in aggregate principal amount at maturity for purchase by us. The purchase price for the LYONs was $584.31 in cash per $1,000 in principal amount at maturity. The aggregate purchase price for all the LYONs validly surrendered for purchase was $379.7 million. At December 31, 2005, there remains outstanding $80.1 million in aggregate principal amount at maturity and an accreted balance of $48.3 million for the LYONs. The LYONs are uncollateralized and unsubordinated, and rank equal in right of payment to our existing and future uncollateralized and unsubordinated indebtedness.

At the option of the holders, we may be required to purchase all, or a portion, of the remaining LYONs on June 12, 2006 at $608.04 for each note with face value of $1,000. Accordingly, $48.3 million is included in the current portion of long-term debt in the Consolidated Balance Sheet at December 31, 2005, and in the Less than 1 year column in the table of Contractual Obligations, above.

We had various other notes payable totaling $7.0 million at December 31, 2005.

Long-term debt, other than the LYONs, has been reflected in the table above at its stated maturity dates for presentation purposes only. On specified dates, our repayment obligation could occur earlier than the maturity dates presented above because holders of the debentures have the right to require us to repurchase the debt.

(2) In July 2003, we entered into a new six-year lease to rent a research and development facility in Emeryville, California (R&D Property) following the expiration of the existing lease accounted for as an operating lease. We accounted for this new lease as a capital lease and, as a result, recorded the leased asset and the corresponding liability of $157.5 million on our balance sheet. This amount represents the present value of minimum lease payments, including the residual value guarantee. The lease provides a $156.0 million residual value guarantee from us to the lessors in the event fair value of the R&D Property declines below the total investment of $173.3 million made by the lessors in the R&D Property. Consequently, our maximum payment obligation is $156.0 million upon termination of the lease on or before July 1, 2009. When the lease agreement includes a residual value guarantee, we use the following method to estimate amortization of the leased asset. First we determine the amount that may become payable to the lessor at the end of the lease term due to a decline in the estimated fair value of the leased asset below the lessor s total investment of $173.3 million. The leased asset is then amortized using a straight-line method to an amount such that the capital lease liability, net of the book value of the amortized leased asset at the end of the lease term equals the amount payable to the lessor. We estimated the fair value of the R&D Property at the end of the lease term will be approximately $168.9 million. The fair value at the end of the lease term was estimated using the cost approach in which appraised value at lease inception is modified by estimates for

building cost appreciation and building component depreciation through the six-year lease term. This valuation requires significant estimates and assumptions. We believe the fair value assigned is based on reasonable assumptions. Aggregate amortization of the leased asset over the term of the lease is estimated to be approximately $6.0 million. For the years ended December 31, 2005, 2004 and 2003, $1.0 million, $1.0 million and $0.5 million, respectively, were recorded as amortization expense for the capital lease.

At the inception of the lease, the future minimum lease payments, exclusive of a residual value guarantee, are approximately $15.7 million over the lease term. The lease payments represent variable-rate interest payments indexed to a three-month London interbank offered rate plus 40 basis points. On or before July 1, 2009, we can choose to either purchase the facility from the lessors or sell the facility to a third party. This option accelerates if we default on our lease payments or in the event of other defined events. If we choose to purchase the facility from the lessors the specified purchase consideration under the lease agreement is $173.3 million. Novartis has guaranteed (under provisions of the Investment Agreement) payments on this lease commitment, including payment of the residual value guarantee, to a maximum of $175.0 million.

(3) Other non-current liabilities as recorded in the Consolidated Balance Sheet as of December 31, 2005.

(4) We lease laboratory, office and manufacturing facilities, land and equipment under noncancelable operating leases, which expire through 2015.

(5) Effective August 1, 2003, Chiron and IBM Corporation amended and restated the previous ten-year information technology services agreement which was effective on July 1, 1998. Under this revised agreement, IBM agreed to provide us with a full range of information services until March 31, 2010. We can now terminate this agreement, subject to certain termination charges. At December 31, 2005, minimum future payments to IBM are expected to be approximately $39.6 million. Payments to IBM are subject to adjustment depending upon the levels of services and infrastructure equipment provided by IBM, as well as inflation.

(6) We had noncancelable purchase orders for ongoing operations of $74.2 million at December 31, 2005.

(7) In connection with the production of our influenza vaccine products, we must purchase large quantities of incubated fertile chicken eggs. Currently, for FLUVIRIN® influenza vaccine, we purchase those eggs and incubation services from a single supplier in the United Kingdom and, pursuant to the contract with that supplier, we have agreed to make specified purchases of 10.6 million British Pounds ($18.3 million at December 31, 2005) each year from that supplier through 2012, subject to our right to terminate this agreement earlier upon payment of a termination fee. To ensure that the incubation of the eggs is the appropriate standard for vaccine manufacturing, we acquired assets of the primary incubation facility from the egg supplier in December 2005.

(8) In 2003, our Board of Directors approved $50.7 million in expenditures for a 25-year building lease and $42.2 million for capital improvements, both of which are part of a $97.0 million project for expansion and replacement of our influenza vaccines primary manufacturing facility in Liverpool, United Kingdom. The new manufacturing facility will replace a portion of the existing influenza vaccines manufacturing facilities in Liverpool, United Kingdom and is anticipated to be available in 2009 for the manufacture of influenza vaccines, subject to regulatory approval. In December 2003, we entered into a 25-year lease for the building. As of December 31, 2005, we have incurred $23.0 million for the capital improvements portion of the project.

(9) In April 2001, Chiron, Rhein Biotech N.V. (now part of Berna Biotech) and GreenCross Vaccine Corporation entered into a collaboration to research and develop certain pediatric combination vaccine products for sale outside of Europe and North America. The collaboration agreement requires capital commitments from Chiron, Berna Biotech and Green Cross Vaccine. Our

commitment is approximately 34.6 million Euro ($41.0 million at December 31, 2005) for the expansion of our Italian manufacturing facilities, of which we had incurred costs of 33.9 million Euro ($40.2 million), as of December 31, 2005. This agreement began in the fourth quarter 2001 and is expected to continue through 2006.

(10) We had various other firm purchase and capital project commitments totaling approximately $43.9 million at December 31, 2005.

(11) In 2003, we entered into a four-year Communication Services Agreement with Infonet USA Corporation. The contract requires a minimum monthly payment of $0.1 million and our commitment at December 31, 2005, totaled $2.1 million.

(12) At December 31, 2005, we had $14.8 million committed under letters of credit, which are required by German law, related to ongoing legal proceedings in Germany.

(13) We participate in a number of research and development arrangements with other pharmaceutical and biotechnology companies to research, develop and market certain technologies and products. We and our collaborative partners generally contribute certain technologies and research efforts and commit, subject to certain limitations and cancellation clauses, to share costs related to certain research and development activities, including those related to clinical trials. At December 31, 2005, aggregate annual noncancelable funding commitments under collaborative arrangements are as follows: 2006 $32.0 million and 2007 $10.0 million. There are no noncancelable funding commitments under collaborative arrangements thereafter. We may also be required to make payments to certain collaborative partners upon the achievement of specified milestones. At December 31, 2005, aggregate milestone payments that may become due under these noncancelable collaborative arrangements totaled $9.4 million. These milestone payments are due upon the achievement of various technical milestones, completion of trials and regulatory filings. From the inception of these contracts through December 31, 2005, costs incurred under these collaborative arrangements totaled $71.5 million.

In addition to these collaboration arrangements, we have entered into contracts where we are responsible for all the costs related to research and development activities. At December 31, 2005, aggregate annual noncancelable commitments under these contracts are as follows: 2006 $4.3 million and 2007 $0.6 million. At December 31, 2005, aggregate milestone payments that may become due under these noncancelable arrangements totaled $4.5 million. These milestone payments are due upon the achievement of various technical milestones, completion of trials and regulatory filings. From inception of these contracts through December 31, 2005, costs incurred under these contracts totaled $9.5 million.

The timing of payments required for the achievement of milestones in the future is not determinable, therefore we have included future milestone payments in less than 1 year for presentation purposes.

(14) We had various performance bonds and insurance-related letters of credit in the amount of $21.3 million available at December 31, 2005. There are no amounts outstanding under these letters of credit at December 31, 2005.

(15) Effective February 2003, Chiron and Baxter Pharmaceutical Solutions LLC executed an eight-year manufacturing and supply agreement. Under this agreement, Baxter agreed to perform certain manufacturing procedures and supply us with a key component for a certain biopharmaceutical product. We have certain minimum purchase obligations under this agreement and are required to pay the difference, if any, between the actual quantity purchased and the minimum purchase obligation. We can terminate this agreement after the third year with eighteen month s notice. At December 31, 2005, our minimum purchase obligation under this agreement over the next eighteen months is expected to be $17.5 million.

(16) Effective October 2002, Chiron and Medical Associates Network, Inc., Medimop Medical Projects, Ltd. and Medimop Medical Projects North, Ltd. (referred to as Med Parties in this section) executed a five-year supply agreement. Under this agreement, the Med Parties agreed to provide us with a presentation device for certain pharmaceutical products. We agreed to fund the Med Parties up to $1.5 million through 2003 to acquire the tools and equipment to manufacture the presentation device, of which we have paid $1.5 million as of December 31, 2005. In addition, under this agreement, we have minimum purchase requirements. Our minimum purchase obligation for the next two years is approximately $11.9 million. We can terminate the agreement subject to twelve-months notification. If we do not terminate the agreement by December 31, 2007, the agreement will be automatically renewed for an additional twelve months.

(17) In 2003, we became a limited partner of Burrill Life Sciences Capital Fund, L.P. We agreed to pay $10.0 million over six years, of which $4.7 million has been paid through December 31, 2005 for a 5.14% ownership. The partnership agreement does not allocate the contribution across future years; therefore we have included the remaining contributions in less than 1 year for presentation purposes.

(18) In 2003, we became a limited partner of Forward Venture V, L.P. We agreed to pay $5.0 million over five years, of which $0.6 million has been paid through December 31, 2005, for a 3.45% ownership. The partnership agreement does not allocate the contribution across future years; therefore, we have included the remaining contributions in less than 1 year for presentation purposes.

(19) In 2002, we became a limited partner of TPG Biotechnology Partners, L.P. We agreed to pay $5.0 million over ten years, of which $2.8 million has been paid through December 31, 2005, for a 2.83% ownership. The partnership agreement does not allocate the contribution across future years; therefore, we have included the remaining contributions in less than 1 year for presentation purposes.

(20) In 2001, we became a limited partner of Forward Venture IV, L.P. We agreed to pay $15.0 million over ten years, of which $13.1 million has been paid through December 31, 2005, for a 6.35% ownership. The partnership agreement does not allocate the contribution across future years; therefore, we have included the remaining contributions in less than 1 year for presentation purposes.

(21) In 2000, we became a limited partner of Burrill Biotechnology Capital Fund, L.P. We agreed to pay $25.0 million over five years, of which $21.7 million has been paid through December 31, 2005, for a 23.26% ownership. The partnership agreement does not allocate the contribution across future years; therefore, we have included the remaining contributions in less than 1 year for presentation purposes.

(22) Effective June 2003, Chiron and SynCo B.V., a related party, executed a seven and a half-year contract manufacturing agreement. Under this agreement, SynCo agreed to provide services related to the production of certain of our vaccine products for the European and U.S. markets commencing in 2004. We have a firm binding order for products to be delivered by SynCo in 2006 under this agreement. Our minimum purchase obligation under this agreement, which depends on the quantities purchased by us in years 2007 through 2010, inflation and movement in the Euro to U.S. Dollar exchange rate, is expected to be approximately $20.5 million over the remaining term of the agreement.

(23) In August 2003, we entered into a $2.5 million revolving credit agreement with Nektar Therapeutics to support the financing of equipment, facility improvements and other capital expenditures related to the manufacture of clinical supplies in support of a program to develop a dry powder formulation of TOBI® tobramycin. Each advance made under this revolving line of credit matures on the sixth

anniversary of the initial advance. As of December 31, 2005, Nektar Therapeutics has not drawn from the revolving line of credit.

(24) In March 2004, we entered into a worldwide, exclusive, multi-product, collaborative arrangement with XOMA Ltd. for the development and commercialization of antibody products for the treatment of cancer. Under the terms of the arrangement, the parties agreed to jointly research, develop, and commercialize multiple antibody product candidates. Under the arrangement, the parties agreed to share development and commercialization expenses, including preclinical and clinical development, manufacturing and worldwide marketing costs, as well as revenues, generally on a 70-30 basis, with our share being 70% and XOMA s share being 30%. We agreed to make an initial payment of $10.0 million, which was paid as of December 31, 2004, and to make a loan facility of up to $50.0 million available to XOMA, starting on January 1, 2005 to fund 75% of XOMA s share of development expenses. Under this arrangement, we made $12.1 million in loan advances to XOMA as of December 31, 2005. Interest payable by XOMA is due when the principal is due and is additive to the $50.0 million available principal. Interest payable of $0.3 million was added to the outstanding balance as of December 31, 2005. The loan advances are recorded at their fair value based upon an interest rate for a similar loan facility from a bank to a similar counterparty. The recorded amount will be accreted to full face value over the life of the outstanding facility based on the effective interest method. At December 31, 2005, $7.1 million was recorded as Non-current notes receivable in the Consolidated Balance Sheet for these loan advances. The funding of the loan facility in the future is not determinable; therefore, we have included the entire amount available under the loan facility in less than 1 year for presentation purposes.

(25) Effective June 2002, Chiron and VWR International, Inc. executed a seven-year managed services agreement. Under this agreement, VWR agreed to provide us with purchasing and delivery services. Effective June 2005, we amended this agreement for a new term through 2012. We can terminate this agreement at any time with six month s notice. If we do not terminate this agreement, payments to VWR are expected to be approximately $6.5 million, of which approximately $0.5 million was paid in 2005. Under the amendment, we have the option to renew the agreement for an additional three years at the end of the new termination date in 2012.

Borrowing Arrangements

Our $100.0 million revolving, committed, uncollateralized credit facility with a major financial institution expired in February 2006 and was not renewed at our election. This facility had been guaranteed by Novartis AG under a November 1994 Investment Agreement. There were no borrowings outstanding under this credit facility at December 31, 2005 and 2004. In July 2003, we entered into a new six-year lease to rent a research and development facility in Emeryville, California. Under provisions of the November 1994 Investment Agreement, Novartis AG guaranteed payments on this lease commitment to a maximum of $175.0 million.

Under the terms of the Investment Agreement, Novartis agreed to guarantee certain of our obligations under revolving credit facilities through January 1, 2008, the date on which the guarantee will expire. The principal amount of indebtedness under the guaranteed credit facilities outstanding at any one time may not exceed a specified cap. That cap was $402.5 million. In November 1996, we and Novartis agreed that we could increase the maximum borrowing amount under the guaranteed credit facilities by up to $300.0 million, for a maximum borrowing amount under the cap of $702.5 million. In exchange for this increase, the amount of our common stock required to be purchased by a Novartis affiliate, at our request, under the Subscription Agreement, would be reduced by an equal amount. The maximum amount Novartis is required to guarantee pursuant to the terms of the Investment Agreement has been reduced by $109.8 million following an election by us in December 2005, to exercise our subscription rights under the Investment Agreement, decreasing the cap to $592.7 million. We also agreed to enter into a separate agreement with Novartis for each obligation guaranteed by Novartis under which we agree to reimburse Novartis for any payments made or out-of-pocket expenses incurred by Novartis in connection with the guarantee (each, a Reimbursement Agreement). Our obligations under the Reimbursement Agreements are, at the request of Novartis, to be fully secured by collateral (which means guaranteed by assets pledged by us) acceptable to Novartis. As discussed above, through February 2006, Novartis guaranteed a $100.0 million U.S. credit facility for our benefit for which there were no borrowings outstanding at December 31, 2005 and $173.3 million of our capital lease commitments. The U.S. credit facility has since expired and at our election was not renewed and is thus no longer guaranteed by Novartis. As a result of these guarantees and the conversion of $9.8 million of bonds in 2000 into shares of our common stock, there remains approximately $417.7 million of the guarantee available following the exercise of our subscription rights and our subsequent election to increase the amount Novartis may be required to guarantee to the maximum borrowing amount.

We also have various credit facilities available outside the U.S. There were no outstanding borrowings under these facilities at December 31, 2005 and 2004. One facility is maintained for our 51%-owned Indian subsidiary, and allows for total borrowings of 200 million Indian Rupees ($4.4 million at December 31, 2005). There were no outstanding borrowings under this facility at December 31, 2005 and 2004.

Off-Balance Sheet Arrangements

As of December 31, 2005 and 2004, we do not have any off-balance sheet arrangements.

Market Risk Management

Our cash flow from operations and earnings are subject to fluctuations due to changes in foreign currency exchange rates, interest rates, the fair value of equity securities held and the realized value of investment securities sold. We attempt to limit our exposure to some or all of these market risks through the use of various financial instruments. These activities are discussed in further detail in Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

Factors That May Affect Future Results

As a global biopharmaceutical company, we are engaged in a rapidly evolving and often unpredictable business. The forward-looking statements contained in this Form 10-K and in other periodic reports, press releases, presentations and other statements issued by us from time to time reflect our current beliefs and expectations concerning objectives, plans, strategies, future performance and other future events. The following discussion highlights some of the factors, many of which are beyond our control, which could cause actual results to differ materially.

Chiron will be subject to business uncertainties and contractual restrictions in connection with the proposed merger with Novartis.

Uncertainty about the proposed merger with Novartis and its possible effect on employees, customers and other constituencies have had an adverse effect on Chiron. These uncertainties have impaired our ability to attract, retain and motivate key personnel, and have caused customers, suppliers, partners and others that deal with us to seek to change existing business relationships. Retention of certain employees has been challenging during the pendency of the merger, as employees experience uncertainty about their future roles after the merger or the prospects of Chiron if the merger does not occur. If key employees continue to depart because of issues relating to the uncertainty and difficulty of integration or a desire not to remain with Novartis after the merger or with Chiron if the merger is not consummated, our business could be harmed. In connection with the proposed merger, some distributors, customers and strategic partners could delay or defer decisions, which could negatively impact revenues, earnings and cash flows of Chiron.

In addition, the merger agreement restricts us from taking specified actions without the consent of Novartis, including making certain capital expenditures, entering into material contracts and other matters. These restrictions may prevent us from pursuing attractive business opportunities that may arise prior to the completion of the merger and may impede our growth and limit the development of our projects, which could negatively impact revenues, earnings and cash flows of Chiron.

Developments with respect to influenza vaccines over the past year may harm our business and results of operations.

In October 2004, the U.K. regulatory body, the Medicines and Healthcare products Regulatory Agency, or MHRA, suspended our license to manufacture FLUVIRIN® vaccine at our Liverpool, U.K. facility. As a result of the suspension of our license, we did not release any FLUVIRIN® vaccine during the 2004-2005 influenza season. On March 2, 2005, the MHRA notified us that it had lifted the license suspension, giving Chiron clearance to initiate full production of FLUVIRIN® vaccine, conditioned on the understanding that Chiron s commitment to its remediation plan will continue and will be subject to further inspections by the MHRA. On October 17, 2005, we initiated delivery and release of FLUVIRIN® vaccine to customers in the United States for the 2005-2006 influenza season. As of such time, we had received all necessary approvals from the U.S. Food and Drug Administration (FDA) and MHRA to start supplying FLUVIRIN® vaccine to the U.S. market.

We received a grand jury subpoena issued by the U.S. Attorney s Office for the Southern District of New York in October 2004 requesting production of certain documents relating to FLUVIRIN® vaccine and the suspension by the MHRA of our license. In February 2005, after having previously commenced an informal inquiry, the Securities and Exchange Commission, or SEC, notified us that it would commence a formal investigation into whether we or our employees violated any federal securities laws in connection with these developments regarding FLUVIRIN® vaccine, and Chiron subsequently received subpoenas from the SEC requesting production of certain documents relating to our Liverpool facility and FLUVIRIN® vaccine. In February 2006, the SEC notified us that it had decided to terminate its investigation, and that no enforcement action had been recommended against the company. We also received a voluntary request for information from the United States House of Representatives, Energy and Commerce Committee, Subcommittee on Oversight and Investigations requesting production of certain documents. Numerous documents have been collected and produced in response to these requests, and several witnesses have been interviewed by the U.S. Attorney s Office, the SEC staff and Congressional staff. Additional investigations regarding these matters may arise.

In addition, we and certain of our officers and directors have also been named as defendants in several putative shareholder class action and derivative lawsuits alleging various claims arising out of or relating to these developments regarding FLUVIRIN® vaccine, which are described in Part I, Item 3, Legal Proceedings . Certain distributors and other parties with whom we had contracted to supply FLUVIRIN® vaccine are considering or have communicated claims against us as a result of our inability to supply FLUVIRIN® vaccine, and additional parties may do so in the future. On January 27, 2005, the U.S. Centers for Disease Control and Prevention, or CDC, terminated its contracts with Chiron for the supply of FLUVIRIN® vaccine for default on the basis of Chiron s failure to supply such vaccine to the U.S. government for the 2004-2005 influenza season. The CDC has reserved the right to hold Chiron liable for any excess costs it may have incurred in replacing any FLUVIRIN® vaccine that Chiron failed to deliver and further has reserved all other remedies provided under the contract. It is not possible to predict whether any of these claims will be pursued and, if so, whether those claims will be upheld. Investigations, litigation and disputes have caused us to incur substantial expense and have required significant time and attention from our management and will continue to do so in the future and could result in civil action and/or criminal proceedings against Chiron. The results of any such investigations, proceedings or disputes could have a material adverse effect on our consolidated financial position and results of operations and/or cash flow.

Although the MHRA has lifted its suspension of our license to manufacture FLUVIRIN® vaccine, we expect to incur additional expenses in connection with ongoing FLUVIRIN® vaccine matters, which could be material, including in connection with (1) our continuing remediation efforts at our Liverpool facility; and (2) responding to private lawsuits and other claims and investigations that exist or may arise.

For additional information on the U.S. Attorney s investigation, SEC investigation, private lawsuits and other claims, see Part I, Item 3. Legal Proceedings of this report on Form 10-K.

BEGRIVAC vaccine is manufactured at our facility in Marburg, Germany. In July 2005, we reported that we would be unable to supply any BEGRIVAC vaccine doses for the 2005-2006 influenza season due to a product sterility issue and wrote off our existing product inventory resulting in charges of $18.0 million to cost of sales for the year ended December 31, 2005. Investigation of the product sterility issue has been completed and implementation of remedial measures and facility modifications is underway. Our inability to supply BEGRIVAC vaccine as planned to non-U.S. markets for the 2005-2006 influenza season or, if remedial efforts are delayed or not successful, future seasons could have a material adverse affect on our business and results of operations. In addition, it is possible that distributors and other parties with whom we had contracted to supply influenza vaccine may make claims against us as a result of Chiron not supplying influenza vaccine. Any such claims may cause us to incur substantial expense and require significant time and attention from our management. The results of any such claims could have a material adverse effect on our consolidated financial position and results of operations and/or cash flow.

We did not release any FLUVIRIN® vaccine during the 2004-2005 influenza season. As a result, our results of operations for 2004 were materially adversely affected by these matters. In addition, we did not release any BEGRIVAC vaccine during the 2005-2006 influenza season. Additional issues with respect to influenza vaccines could cause us to have to recognize an impairment charge with respect to the goodwill, certain other intangible assets and property, including without limitation the Liverpool plant resulting from the PowderJect acquisition and the new influenza vaccines manufacturing facility under construction in Liverpool, which could have a material adverse effect on our results of operations.

Our previous inability to supply influenza vaccines has led to loss of market share and may lead to loss of additional market share in future seasons. Following the announcement of our FLUVIRIN® license suspension, competitors announced plans to introduce influenza vaccine products in the United States and

sought expedited regulatory approval to do so. Even though the license suspension has been lifted, some of our customers may continue to choose to purchase influenza vaccine from other providers as their products become available in the United States. Loss of market share in the United States or foreign markets could have a material adverse effect on our business and results of operations. Delays in start-up procedures for ramping up to full production and normal manufacturing issues inherent in the complexity of influenza vaccine production, adversely affected the amount of FLUVIRIN® vaccine that we were able to produce for the 2005-2006 influenza season and may result in further loss of market share.

If we fail to obtain or maintain the regulatory approvals we need to market our products or substantial changes in the regulatory environment occur, our business may suffer.

We must obtain and maintain regulatory approval in order to market most of our products. Generally, these approvals are on a product-by-product and country-by-country basis. In the case of influenza vaccines, the failure to obtain or maintain our licenses, or delays imposed by regulatory actions, could lead to the loss of our entire inventory during any given season since each year s vaccines are manufactured to meet specific strains of influenza. In the case of therapeutic products, a separate approval is required for each therapeutic indication. Product candidates that appear promising based on early, and even large-scale, clinical trials may not receive regulatory approval. Furthermore, the results of clinical trials often are susceptible to varying interpretations that may delay, limit or prevent approval or result in the need for additional pre-marketing or post-marketing studies. In addition, regulations may be amended from time to time. Revised regulations may require us to reformulate products on a country or regional basis, obtain additional regulatory approvals, or accept additional risks that our products will not maintain market acceptance or be eligible for third party insurance coverage. Increased regulatory scrutiny and restrictions regarding marketing practices for products that are subject to government reimbursement may impact the sales of such products. There is no guarantee that we will be able to meet conditions to obtain or maintain regulatory approval or to satisfy new regulatory requirements and may suffer a loss of revenue as a result.

If our focus on the research and development of emerging technologies does not result in the creation of commercial products, our business could be harmed.

We focus our research and development activities on areas in which we have particular strengths and on technologies that appear promising. These technologies often are on the cutting edge of modern science. As a result, the outcome of any research or development program is highly uncertain. Only a very small fraction of these programs ultimately result in commercial products or even product candidates. Product candidates that initially appear promising often fail to yield successful products. In many cases, preclinical or clinical studies will show that a product candidate is not efficacious (that is, it lacks the intended therapeutic or prophylactic effect), or that it raises safety concerns or has other side effects, which outweigh the intended benefit. Success in preclinical or early clinical trials (which generally focus on safety issues) may not translate into success in large-scale clinical trials (which are designed to show efficacy), often for reasons that are not fully understood. Further, success in clinical trials will likely lead to increased investment, adversely affecting short-term profitability, to bring such products to market. And even after a product is approved and launched, general usage or post-marketing studies may identify safety or other previously unknown problems with the product which may result in regulatory approvals being suspended, limited to narrow indications or revoked, or which may otherwise prevent successful commercialization.

Our products are complex and difficult to manufacture on a large-scale basis, which could cause us to delay product launches, experience shortages of products or prevent us from offering products on a volume basis.

Most of our products are biologics and manufacturing biologic products is complex. A biologic product generally cannot be sufficiently characterized (in terms of its physical and chemical properties) to

rely on assaying of the finished product alone to ensure that the product will perform in the intended manner. Accordingly, it is essential to be able to both validate and control the manufacturing process, that is, to show that the process works and that the product is made strictly and consistently in compliance with that process. Slight deviations anywhere in the manufacturing process, including quality control, labeling and packaging, may result in unacceptable changes in the products that may result in lot failures or product recalls, or liability to a third party to the extent we are contract manufacturing products in our facilities for such third party. Manufacturing processes which are used to produce the smaller quantities of material needed for research and development purposes may not be successfully scaled up to allow production of commercial quantities at reasonable cost or at all. All of these difficulties are compounded when dealing with novel biologic products that require novel manufacturing processes. Additionally, manufacturing is subject to extensive government regulation. Even minor changes in the manufacturing process require regulatory approval, which, in turn, may require further clinical studies. For some of our products, we rely on others to supply raw materials and to manufacture those products according to regulatory requirements.

In addition, any prolonged interruption in our operations or those of our partners could result in our inability to satisfy the product demands of our customers. A number of factors could cause interruptions, including equipment malfunctions or failures, interruptions due to labor action, damage to a facility due to natural disasters, such as an earthquake, suspension of power supplied to these facilities arising out of regional power shortages or terrorist activities and armed conflict, including as a result of the disruption of operations of our subsidiaries and our customers, suppliers, distributors, couriers, collaborative partners, licensees and clinical trial sites.

If we are unable to successfully compete in the highly competitive healthcare industry, our business could be harmed.

We operate in a highly competitive environment, and the competition is expected to increase. Competitors include large pharmaceutical, chemical and blood testing companies, compounding pharmacies, and biotechnology companies. Some of these competitors, particularly large pharmaceutical and blood testing companies, have greater resources than us. Accordingly, even if we are successful in launching a product, we may find that a competitive product dominates the market for any number of reasons, including:

- The possibility that the competitor may have launched its product first;
- The competitor may have greater access to certain raw materials;
- The competitor may have more efficient manufacturing processes;
- The competitor may adapt more quickly to technological change;
- The competitor may have greater marketing capabilities;
- The competitive product may have therapeutic or other advantages; or
- New competitors may enter into markets where we currently have significant competitive advantage.

The technologies applied by our competitors and us are rapidly evolving, and new developments frequently result in price competition and product obsolescence. In addition, we may be impacted by competition from generic forms of our products, substitute products or imports of products from lower priced markets.

Our work on new vaccines for pandemic preparedness exposes us to special risks that we may be unable to control.

We continue to incur significant expenses in researching, developing and manufacturing new vaccines for pandemic preparedness. To date, these vaccines have undergone limited clinical testing and are not approved for use outside of clinical trials. In the event of a pandemic, countries may opt to use our pandemic vaccines without full clinical trials. Although there is some effort to limit product liability exposure for manufacturers of pandemic vaccines, we cannot be assured that any attempts to limit liability exposure, whether legislatively or contractually, will sufficiently address our risks or be adopted in all countries.

In addition, a pandemic or the perceived risk of a pandemic could result in countries taking actions to protect their citizens that could affect our ability to control the production and export of pandemic vaccines or otherwise impose burdensome regulations on our business. For example, our manufacturing locations may be subject to possible seizure by governments in the event of a pandemic. Countries may also require that we grant compulsory licenses to allow competitors to manufacture products that are covered by our patents. Although we have entered into agreements to provide vaccine to certain countries where our manufacturing facilities are located, we cannot give any assurance that these agreements will prevent actions that decrease our sales or otherwise harm our business.

Conflicts with or decisions by third parties we collaborate with could harm our business.

An important part of our business strategy depends upon collaborations with third parties, including research collaborations and joint efforts to develop, commercialize new products and manufacture, market and distribute existing products. As circumstances change, Chiron and our strategic partners may develop conflicting priorities or other conflicts of interest or decide not to extend existing collaborations. We may experience significant delays and incur significant expenses in resolving these conflicts and may not be able to resolve these matters on acceptable terms. Even without conflicts of interest, we may disagree with our strategic partners as to how best to realize the value associated with a current product or a product in development. In some cases, the strategic partner may have responsibility for formulating and implementing key strategic or operational plans. In addition, merger and acquisition activity within the pharmaceutical and biotechnology industries may affect our strategic partners, causing them to reprioritize their efforts related to the research collaborations and other joint efforts with us. Decisions by corporate partners on key clinical, regulatory, marketing (including pricing), inventory management and other issues may prevent successful commercialization of the product or otherwise impact our profitability.

If any of our third party suppliers or manufacturers cannot adequately meet our needs, our business could be harmed.

We use raw materials and other supplies that generally are available from multiple commercial sources. Certain manufacturing processes, however, use materials that are available from sole sources, or that are in short supply, or are difficult for the supplier to produce and certify in accordance with our specifications. From time to time, concerns are raised with respect to potential contamination of biological materials that are supplied to us. These concerns can further tighten market conditions for materials that may be in short supply or available from limited sources. Moreover, regulatory approvals to market our products may be conditioned upon obtaining certain materials from specified sources. Our ability to substitute material from an alternate source may be delayed pending regulatory approval of such alternate source. Although we work to mitigate the risks associated with relying on sole suppliers, there is a possibility that material shortages could impact production.

We purchase bulk powdered tobramycin, the primary basic raw material in TOBI® tobramycin, from two of the principal worldwide suppliers of the drug. We anticipate that either one of these suppliers alone

will be able to supply sufficient quantities to meet current needs; however, there can be no assurance that these suppliers will be able to meet future demand in a timely and cost-effective manner. As a result, our operations could be adversely affected by an interruption or reduction in the supply of bulk tobramycin powder.

We have entered into contracts with third parties for the production and packaging of TOBI® tobramycin. Over time, we can use alternative production and packaging sources. However, if the contracted third parties become unable to produce or package sufficient quantities of TOBI® solution due to work stoppages or other factors, our operations could be disrupted until alternative sources are secured. We have entered into contracts with third parties for the packaging of the pre-filled diluent syringe for BETASERON® interferon beta-1b. Over time, we can use alternative packaging sources. However, if the contracted third parties become unable to produce or package sufficient quantities of the pre-filled diluent syringe for BETASERON® interferon beta-1b due to work stoppages or other factors, our operations could be disrupted until alternative sources are secured.

In connection with the production of our influenza vaccine products, we must purchase large quantities of incubated fertile chicken eggs. Currently, for FLUVIRIN® influenza vaccine, we purchase those eggs from a single supplier in the United Kingdom and, pursuant to the contract with that supplier, we have agreed to make specified purchases from that supplier through 2012, subject to our right to terminate this agreement earlier upon payment of a termination fee. To ensure that the incubation of the eggs is of the appropriate standard for vaccine manufacturing, we acquired the assets of the primary incubation facility from the egg supplier in December 2005. Avian influenza has resulted in the massive death or culling of domestic poultry in certain regions, primarily Southeast Asia. If our suppliers were to fail to supply eggs in sufficient quantities or quality, including as a result of any outbreak of avian influenza or other issues related to the chickens, our business would be materially affected.

We are a key provider for the blood screening field of nucleic acid testing and immunodiagnostics. In nucleic acid testing, we rely on our collaborative partner, Gen-Probe, to manufacture the PROCLEIX® WNV Assay, currently in use on an investigational-use basis in the U.S., and the PROCLEIX® HIV-1/HCV Assay and PROCLEIX® ULTRIO® Assay. The related instrument systems are sourced from third party suppliers. Currently, Gen-Probe is the only manufacturer of nucleic acid testing products using Transcription-Mediated Amplification technology. In immunodiagnostics, under our joint business contractual arrangements with Ortho-Clinical Diagnostics, we manufacture bulk reagents and antigens and confirmatory test kits sold in the clinical diagnostics and blood screening fields. While we and our partners work to mitigate the risks associated with being a key provider, there can be no assurance that our partner, Gen-Probe, will be able to provide sufficient quantities of the PROCLEIX® WNV Assay, PROCLEIX® HIV-1/HCV Assay and PROCLEIX® ULTRIO® Assay or that we will be able to manufacture sufficient bulk reagents and antigens and confirmatory test kits for immunodiagnostic products. Our difficulties or delays or those of our partners could cause a public health concern for the blood supply, as well as increase costs and cause loss of revenue or market share.

If we cannot obtain necessary licenses to third party patents for the manufacture or sale of our products, we may have to withdraw from the market or delay the introduction of the affected product.

Third parties, including competitors, have patents and patent applications in the U.S. and other significant markets that may be useful or necessary for the manufacture, use or sale of certain products and products in development by our strategic partners and us. It is likely that third parties will obtain these patents in the future. Certain of these patents may be broad enough to prevent or delay us and our strategic partners from manufacturing or marketing products important to our current and future business. We cannot accurately predict the scope, validity and enforceability of these patents, if granted, the extent to which we may wish or need to obtain licenses to these patents, and the cost and availability of these

licenses. If we do not or cannot obtain these licenses, products may be withdrawn from the market or delays could be encountered in market introduction while an attempt is made to design around these patents, or we could find that the development, manufacture or sale of such products is foreclosed. We could also incur substantial costs in licensing or challenging the validity and scope of these patents.

Because most of our products are based on technologies that are unfamiliar to the healthcare community, they may not be accepted by healthcare providers and patients, which could harm our business.

We may experience difficulties in launching new products, many of which are novel products based on technologies that are unfamiliar to the healthcare community. We have no assurance that healthcare providers and patients will accept such products. In addition, government agencies, as well as private organizations involved in healthcare, from time to time publish guidelines or recommendations to healthcare providers and patients. Such guidelines or recommendations can be very influential and may adversely affect the usage of our products directly (for example, by recommending a decreased dosage of our product in conjunction with a concomitant therapy or a government entity withdrawing its recommendation to screen blood donations for certain viruses) or indirectly (for example, by recommending a competitive product over our product).

If we are unable to avoid significant exposure to product liability claims, our business could be harmed.

We are exposed to product liability and other claims in the event that the use of our products is alleged to have resulted in adverse effects. While we will continue to take precautions, we may not avoid significant product liability exposure. Although we maintain product liability insurance, there is no guarantee that this coverage will be sufficient. It is not feasible to obtain adequate insurance coverage for certain products and we are self-insured in relation to these products. If we are sued for any injury caused by our products, we could suffer a significant financial loss.

As we are a key provider for the blood screening field of nucleic acid testing and immunodiagnostics, we may have product liability in addition to contract exposure in the event that our difficulties or delays or those of our partners could cause a public health concern for the blood supply.

Sales of our products and profitability may be adversely affected by pricing policies and applicable laws and the availability and amount of reimbursement from third parties, such as the government and insurance companies.

In the U.S., Europe and other significant markets, sales of our products and our profitability may be affected by the pricing policies and applicable laws of, and the availability and amount of reimbursement from, the government or other third parties, such as insurance companies. It is difficult to predict the pricing and reimbursement status of newly approved, novel biotechnology products, and it may be challenging to meet the current pricing and reimbursement policies for existing products, which may be complex, subject to change and limit our revenues. In certain foreign markets, governments have issued more extensive regulations relating to the pricing and profitability of pharmaceutical companies, which can be expected to limit our revenues from certain products. There have been proposals in the U.S. (at both the federal and state level) to implement such controls. If the United States Congress enacts legislative proposals addressing parallel importation currently being deliberated, revenues from certain products may be affected further by this change in U.S. policy. The growth of managed care in the U.S. also has placed pressure on the pricing of healthcare products. These pressures can be expected to continue.

If we market products in a manner that violates state, federal or foreign laws that govern pharmaceuticals and health care products, including FDA, FTC, and health care fraud and abuse laws, we may be subject to civil or criminal penalties, including the potential for exclusion from federal, state and foreign programs.

The federal laws and regulations administered by the FDA and FTC place restrictions on the promotion of medical products. FDA law and regulations prohibit the marketing and promotion of unapproved drug and device products and unapproved uses of approved drug and device products. FTC and FDA also place restrictions on the promotion of approved drugs and devices to ensure that marketing material is not false or misleading. In addition to these restrictions on the marketing of pharmaceutical products without regulatory approval, other types of state and federal health care fraud and abuse laws have been applied in recent years to restrict certain marketing practices in the healthcare industry, and to otherwise determine the eligibility of pharmaceutical manufacturers to have their products reimbursed by Medicare, Medicaid, and other federal and state programs. These laws include anti-kickback statutes, false claims statutes, and others. In addition, the foreign business operations of Chiron are impacted by certain United States laws and regulations. These include prohibitions on payments to foreign officials and restrictions on exports to certain foreign nations or commerce with certain debarred parties. Likewise, various foreign laws may restrict the manner in which healthcare products are marketed in other countries.

The federal anti-kickback statute prohibits, among other things, knowingly offering, paying, soliciting, or receiving remuneration to induce or in return for purchasing, ordering, recommending, or arranging for the purchase, order, or lease of any health care item reimbursable under Medicare, Medicaid, or other federally funded health care programs. This statute has been interpreted broadly to apply to arrangements between drug manufacturers on one hand and prescribers, purchasers, pharmacies, Group Purchasing Organizations, and pharmacy benefit and formulary managers on the other, along with such indirect purchasers as health plans. Although there are a number of statutory exemptions and regulatory safe harbors protecting certain activities from prosecution, the exemptions and safe harbors are drawn narrowly. Activities that fall outside of a safe harbor are not necessarily illegal, but practices that involve direct or indirect remuneration intended to induce prescribing, purchasing, or recommending of products may be subject to governmental scrutiny if they do not qualify for an exemption or safe harbor. Our practices may not in all cases meet all of the criteria for safe harbor protection from anti-kickback liability.

Federal false claims laws generally prohibit a person from knowingly presenting, or causing to be presented, a false claim for payment to the federal government, or knowingly making, or causing to be made, a false statement to have a false claim paid. Recently, several pharmaceutical and other health care companies have been subject to investigative and enforcement activity under these laws, including qui tam suits filed by whistleblowers, for a variety of alleged inappropriate promotional and marketing activities, such as providing free product to customers with the expectation that the customers would bill federal programs for the product; engaging in off-label promotion that caused claims to be submitted to federal and state programs for non-covered off-label uses; and submitting inflated best price and otherwise incorrect pricing data for Medicaid rebate or other price reporting purposes. In some cases, the manufacturers have been alleged to have aided and abetted in the submission of false claims. In addition, state Attorneys General and private class action plaintiffs have filed civil suits under the federal RICO statute and a variety of state consumer protection laws claiming that pharmaceutical companies reported inflated average wholesale prices to pricing services used by the federal programs to set reimbursement rates, and that as a result, Medicare beneficiaries, Medicaid programs and private payers overpaid for drugs. Still other manufacturers have been subject to enforcement activity for alleged violations of such federal statutes as the Prescription Drug Marketing Act, involving pharmaceutical sampling practices. The majority of states also have statutes or regulations similar to the federal anti-kickback law and false claims laws, which apply to items and services, reimbursed under Medicaid and other state programs, or, in several states, apply regardless of the payor.

Sanctions under federal, state and foreign laws may include civil monetary penalties, exclusion of a manufacturer s products from reimbursement under government programs, criminal fines, and imprisonment. Because of the breadth of these laws and the narrowness of the safe harbors, it is possible that some of our business activities could be subject to challenge under one or more of such laws.

Our mishandling of hazardous materials could result in substantial costs and harm to our business.

In connection with our research and manufacturing activities, we utilize some hazardous materials. We believe we take great care to ensure we have appropriate procedures and permits in place for storing and handling such hazardous materials. We could be subject to loss of our permits, government fines or penalties and/or other adverse governmental action if such hazardous materials are stored, handled or released into the environment in violation of law or any permit. A substantial fine or penalty, the payment of significant environmental remediation costs or the loss of a permit or other authorization to operate or engage in our ordinary course of business could result in material, unanticipated expenses and the possible inability to satisfy customer demand.

Our patents may not prevent competition or generate revenues.

We seek to obtain patents on many of our inventions. Without the protection of patents, competitors may be able to use our inventions to manufacture and market competing products without being required to undertake the lengthy and expensive development efforts made by us and without having to pay royalties or otherwise compensate us for the use of the invention. We have no assurance that patents and patent applications owned or licensed to us will provide substantial protection. Important legal questions remain to be resolved as to the extent and scope of available patent protection for biotechnology products and processes in the U.S. and other important markets. We do not know how many of our pending patent applications will be granted, or the effective coverage of those that are granted. In the U.S. and other important markets, the issuance of a patent is neither conclusive as to its validity nor the enforceable scope of its claims. We have engaged in significant litigation to determine the scope and validity of certain of our patents and expect to continue to do so. An adverse outcome of litigation could result in the reduction or loss of royalty revenues. Engaging in patent litigation against one party may place significant royalty revenues received or to be received from other parties at risk. Even if we are successful in obtaining and defending patents, there can be no assurance that these patents will provide substantial protection. The length of time necessary to resolve patent litigation successfully may allow infringers to gain significant market advantage. Third parties may be able to design around the patents and develop competitive products that do not use the inventions covered by our patents. Many countries, including certain countries in Europe, have compulsory licensing laws under which a patent owner may be compelled to grant licenses to third parties (for example, the third party s product is needed to meet a threat to public health or safety in that country, or the patent owner has failed to work the invention in that country, or the third party has patented improvements). In addition, most countries limit the enforceability of patents against government agencies or government contractors. In these countries, the patent owner may be limited to monetary relief and may be unable to enjoin infringement, which could materially diminish the value of the patent. In addition, royalty revenues may decline as patents expire.

If our efforts to integrate acquired or licensed businesses or technologies into our business are not successful, our business could be harmed.

As part of our business strategy, we expect to continue to grow our business through in-licensing, collaborations or acquisitions of products or companies. The failure to adequately address the financial, operational or legal risks raised by such transactions could harm our business. Financial aspects related to these transactions may alter our financial position, reported operating results or stock price, and include:

- Use of cash resources;

- Potentially dilutive issuances of equity securities;

- The incurrence of debt and contingent liabilities, impairment losses or restructuring charges;

- Large write-offs and difficulties in assessment of the relative percentages of in-process research and development expense that can be immediately written off as compared to the amount which must be amortized over the appropriate life of the asset;

- Amortization expenses related to other intangible assets; and

- Impairment of the value of tangible and intangible assets resulting from management s decision to discontinue a line of business or product previously acquired by Chiron or from changes in business conditions.

Operational risks that could harm our existing operations or prevent realization of anticipated benefits from such transactions include:

- Challenges associated with managing an increasingly diversified business and international business;

- Difficulties in assimilating the operations, products, technology, information systems or personnel of the acquired company;

- Diversion of management s attention from other business concerns;

- Inability to maintain uniform standards, controls, procedures and policies;

- The assumption of known and unknown liabilities of the acquired company, including intellectual property claims; and

- Subsequent loss of key personnel.

Legal risks may include requirements to obtain the consent of our stockholders or a third party, or the approval of various regulatory authorities.

If such efforts to integrate acquired or licensed businesses or technologies into our business are not successful, our business could be harmed.

If we cannot initiate and maintain revenue-generating relationships with third parties, we may not be able to grow our revenues in the near to medium-term.

Many products in our current pipeline are in relatively early stages of research or development. Our ability to grow earnings in the near- to medium-term may depend, in part, on our ability to initiate and maintain other revenue generating relationships with third parties, such as licenses to certain of our technologies, and on our ability to identify and successfully acquire rights to later-stage products from third parties. We may fail to establish such other sources of revenue.

Our international sales and operations involve additional risks that could increase our expenses, adversely affect our operating results and require increased time and attention of our management.

We derive a substantial portion of revenue from sales outside of the U.S. and have significant research, development, manufacturing and marketing operations outside of the U.S. Our planned growth is contingent upon the successful expansion of our international revenue. These international operations are subject to risks in addition to those faced by our U.S. operations, including:

- Fluctuations in currency exchange rates and economic instability such as higher interest rates and inflation;

- Difficulties in hedging foreign currency transaction exposures;

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- Difficulties in staffing, managing, training and operating our international operations;
- Difficulties in coordinating the activities of our geographically dispersed and culturally diverse operations;
- Costs and delays associated with coordinating operations in multiple languages;
- Potential loss of proprietary information due to laws that may be less protective of our intellectual property rights; and
- Exposure to different and evolving legal standards (particularly with respect to product marketing, pricing and competition).

Our level of debt could limit cash flow available for our operations and could adversely affect our ability to service our debt or obtain additional financing, if necessary.

As of December 31, 2005, our total debt including current portion, was $940.3 million. Our level of debt could restrict our operations and make it more difficult for us to satisfy our obligations under the 2033 and the 2034 convertible debentures (the debentures). Among other things, our level of debt may:

- Limit our ability to obtain additional financing for working capital, capital expenditures, strategic acquisitions and general corporate purposes;
- Require us to dedicate all or a substantial portion of our cash flow to service our debt, which will reduce funds available for other business purposes, such as capital expenditures or acquisitions;
- Limit our flexibility in planning for or reacting to changes in the markets in which we compete;
- Place us at a competitive disadvantage relative to our competitors with less leverage;
- Render us more vulnerable to general adverse economic and industry conditions; and
- Make it more difficult for us to satisfy our financial obligations, including those relating to the debentures and our other debt obligations.

We and our subsidiaries may still be able to incur substantially more debt. The terms of the indenture governing the debentures and the agreements governing our other debt permit additional borrowings. Our incurrence of additional debt could further exacerbate the risks described above.

Our ability to satisfy our obligations under the debentures and our other debt agreements will depend on our future operating performance, which will be subject, in part, to factors beyond our control, including general economic and business conditions. If we are unable to generate sufficient cash flow to service our debt, we may be required to refinance all or a portion of our debt, including the debentures, obtain additional financing, sell some of our assets or operations, reduce or delay capital expenditures, or revise or delay our strategic plans. If we are required to take any of these actions, it could have a material adverse effect on our business, financial condition and results of operations. In addition, we cannot assure you that we would be able to take any of these actions, that these actions would enable us to continue to satisfy our capital requirements or that these actions would be permitted under the terms of our various debt instruments, including the indenture governing the debentures.

Our relationship with Novartis AG could limit our ability to enter into transactions or pursue opportunities in conflict with Novartis and could cause the price of our common stock to decline.

On October 30, 2005, we entered into a merger agreement with Novartis AG and Novartis Corporation, pursuant to which Chiron would become a wholly owned subsidiary of Novartis Corporation if the proposed merger is consummated. Apart from the transactions contemplated by the merger agreement, we have an alliance with Novartis AG, a life sciences company headquartered in Basel,

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Switzerland. Under a series of agreements between Chiron and Novartis, which will continue in force while our merger with Novartis is pending or if the merger is not completed, and as a result of subsequent stock issuances by Chiron, Novartis ownership interest in Chiron was approximately 43.9% as of December 31, 2005. The governance agreement between Chiron and Novartis contains provisions that require the approval of Novartis before we enter into certain corporate transactions. These transactions generally include significant debt or equity issuances, debt or equity repurchases, most mergers and acquisitions, the payment of cash dividends, amendments to Chiron s certificate of incorporation or by-laws, and other transactions that would adversely impact the rights of Novartis, or discriminate against Novartis, as a Chiron stockholder. In addition, a majority of the independent directors must approve any material transactions between Chiron and Novartis. These provisions may limit our ability to enter into transactions with third parties otherwise viewed as beneficial to Chiron. In addition, as discussed under *Chiron will be subject to business uncertainties and contractual restrictions in connection with the proposed merger with Novartis*, our merger agreement with Novartis contains additional and more restrictive limitations on our operations while the merger agreement is in effect. All of our shares owned by Novartis are eligible for sale in the public market subject to compliance with the applicable securities laws. We have agreed that, upon Novartis request, we will file one or more registration statements under the Securities Act in order to permit Novartis to offer and sell shares of our common stock, including shares that Novartis was required to purchase from us pursuant to the exercise of our subscription rights under the subscription agreement. Sales of a substantial number of shares of our common stock by Novartis in the public market could adversely affect the market price of our common stock.

Our stock price could be volatile.

The price of our stock, like that of other pharmaceutical companies, is subject to significant volatility. Any number of events, both internal and external to us, may affect our stock price. These include, without limitation:

- Developments with respect to the proposed merger with Novartis;
- Fluctuations in earnings from period to period;
- Results of clinical trials conducted by us or by our competitors;
- Announcements by us or our competitors regarding product development efforts, including the status of regulatory approval applications;
- Impact from the recent influenza vaccines developments;
- The outcome of legal proceedings, including claims filed by us against third parties to enforce our patents and claims filed by third parties against us relating to patents held by the third parties;
- The launch of competing products;
- The resolution of (or failure to resolve) disputes with strategic partners;
- Corporate restructuring by us;
- Adoption of new U.S or foreign laws;
- The sale of a substantial number of shares held by our existing stockholders;
- Licensing activities by us; and
- The acquisition or sale by us of products, products in development or businesses.

In connection with our research and development collaborations, from time to time we may invest in equity securities of our strategic partners. The price of these securities also is subject to significant volatility

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and may be affected by, among other things, the types of events that affect our stock. Changes in the market price of these securities may impact our profitability.

We are subject to taxation in a number of jurisdictions and changes to the corporate tax rate and laws of any of these jurisdictions could increase the amount of corporate taxes we have to pay.

We pay taxes principally in the U.S., Germany, Italy, and the United Kingdom. All of these jurisdictions have in the past and may in the future make changes to their corporate tax rates and other tax laws, which could increase our future tax provision. Specifically, on October 22, 2004, the American Jobs Creation Act of 2004 (the Act) was signed into law. The Act includes an elimination of the tax benefit of the Extraterritorial Income Exclusion over 2005 and 2006.

We have negotiated a number of rulings regarding income and other taxes that are subject to periodic review and renewal. If such rulings are not renewed or are substantially modified, income taxes payable in particular jurisdictions could increase. While we believe that all material tax liabilities are reflected properly in our balance sheet, we are presently under audit in several jurisdictions and may be subject to further audits in the future, and we have no assurance that we will prevail in all cases in the event the taxing authorities disagree with our interpretations of the tax law. In addition, we have assumed liabilities for all income taxes incurred prior to the sales of our former subsidiaries, including PowderJect Vaccines, Inc., SBL Vaccin AB, and PowderJect Research Limited. Future levels of research and development spending, capital investment and export sales will impact our entitlement to related tax credits and benefits which have the effect of lowering our effective tax rate.

In the fourth quarter of 2005, the German tax authorities released draft administrative guidance related to 2003 legislation regarding certain intercompany debt arrangements. We believe that the 2003 legislation as written permits a tax deduction for the interest expense accrued on certain intercompany loans related to our operations in Germany. However, if the 2005 draft administrative guidance is finalized as introduced, intercompany interest expense of approximately $32.0 million per year could be disallowed for the years 2004 and forward, which would have a material adverse impact on our reported effective tax rate. We have not provided for any additional tax since we believe it is currently not probable of payment as this guidance is in draft form and is subject to significant revision.

The ability to use certain deferred tax assets is dependent upon future profitability in the Vaccines business.

A material portion of our deferred tax assets are due to tax loss carryforwards and other deferred tax benefits incurred in the Vaccines business in the UK and Italy, primarily due to reduced FLUVIRIN® influenza vaccine sales and continuing research and development expenses. The ability to use these deferred tax assets is dependent upon us earning sufficient future profits in these jurisdictions. If management determines that profits will not be earned in the tax periods before which such losses expire, then a valuation allowance could be required and a substantial tax expense may result.

Our earnings results may be inconsistent and cause volatility in our stock price.

Our operating results may vary considerably from quarter to quarter. Any number of factors may affect our quarterly operating results. These factors include, but are not limited to the following:

- Inventory management practices, including wholesale ordering patterns;
- The level of pre-clinical and clinical trial-related activities;
- Seasonality of certain vaccine products;
- The tender driven nature of certain vaccine products;
- The nature of our collaborative, royalty and license arrangements and other revenue sources;

- Foreign currency exchange rate fluctuations;
- Effective tax rate fluctuations; and
- The level of product reserves due to various issues, including seasonality patterns, excess and obsolete inventory, and production yields.

Our results in any one quarter are not necessarily indicative of results to be expected for a full year.

Revisions to accounting standards, financial reporting and corporate governance requirements and tax laws result in changes to our standard practices and will impact our results and could require a significant expenditure of time, attention and resources, especially by senior management.

We must follow accounting standards, financial reporting and corporate governance requirements and tax laws set by the governing bodies and lawmakers in the U.S. and other countries where we do business. From time to time, these governing bodies and lawmakers implement new and revised rules and laws. These new and revised accounting standards, financial reporting and corporate governance requirements and tax laws may require changes to our financial statements, the composition of our board of directors, the composition, responsibility and manner of operation of various board-level committees, the information filed by us with the governing bodies and enforcement of tax laws against us. Implementing changes required by such new standards, requirements or laws likely will require a significant expenditure of time, attention and resources, especially by our senior management. It is impossible to completely predict the impact, if any, on Chiron of future changes to accounting standards, financial reporting and corporate governance requirements and tax laws.

It is possible that the application of certain current accounting standards may change due to environmental factors, which may necessitate a change in our standard practice related to these accounting standards. In particular, effective January 1, 2006 we are required to adopt SFAS No. 123(R), which requires us to apply a fair-value based method to account for costs related to share-based payments including stock options and employee stock purchase plans. We expect the adoption of SFAS 123(R) to materially impact our results of operations.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Risk

A significant portion of our operations consists of manufacturing and sales activities in western European countries. As a result, our financial results may be affected by changes in the foreign currency exchange rates of those countries. Our primary exposures to foreign exchange rates are associated with the value of the Euro and the value of the British Pound. To mitigate foreign currency exchange risks, we enter into foreign currency forward contracts and purchase foreign currency option contracts. We do not use any of these derivative instruments for trading or speculative purposes. The total notional amount of these derivative financial instruments at December 31, 2005 and 2004 was $178.2 million and $131.3 million, respectively.

We use foreign currency forward contracts to hedge the gains and losses generated by the re-measurement of certain assets and liabilities denominated in foreign currencies. Typically, these contracts have maturities of three months or less. At December 31, 2005, our transaction exposures amounted to $178.6 million and were offset by foreign currency forward contracts with a notional amount of $178.2 million. The unrealized gain on outstanding foreign currency forward contracts was $2.6 million at December 31, 2005. The notional amount of the foreign currency forward contracts was $131.3 million at December 31, 2004. The unrealized loss on outstanding foreign currency forward contracts was $10.4 million at December 31, 2004. Based on exposures at December 31, 2005, a 10% movement against our portfolio of transaction exposures and hedge contracts would result in a gain or loss of approximately

$0.04 million. A 10% movement in the value of the U.S. Dollar versus our portfolio of transaction exposures has not occurred in the last 12 quarters. Foreign currency gains (losses) from continuing operations, including the impact of hedging, were $1.5 million, $(0.4) million and $5.5 million in 2005, 2004 and 2003, respectively.

Our primary anticipated exposures result from non-U.S. Dollar denominated revenues and expenditures related to our Western European operations. Our risk is that the value of the British Pound increases (i.e., we have a short British Pound exposure) and that the value of the Euro decreases (i.e., we have a long Euro exposure). Our short British Pound exposure is currently larger than our long Euro exposure. Hence, a decrease in the value of the U.S. Dollar vis-à-vis both these currencies will likely have a negative impact on our financial results. We may selectively hedge anticipated currency exposures by purchasing foreign currency option contracts and forward contracts. We may also purchase British Pound denominated fixed income securities to hedge our short British Pound exposure. At December 31, 2005, we had purchased 11.2 million British Pound denominated fixed income securities. When we use options, we usually purchase out-of-the-money foreign currency option contracts to limit hedging costs. At December 31, 2005 and 2004, we had no outstanding option contracts. Based on estimated exposures and existing hedges at December 31, 2005 and based on historical patterns of exchange rate movements, a value-at-risk analysis estimates that there is a 95% probability that our portfolio of anticipated currency exposures will result in a loss of less than $12.7 million over the next 12 months. We may enter into foreign currency forwards or options, or we may buy additional British Pound denominated fixed income securities to hedge these exposures.

Interest Rate Risk

We have exposure to changes in interest rates in both our investment portfolio and certain floating rate liabilities and lease commitments where interest rates are tied to the London Inter-Bank Offered Rate. Our investment portfolio consists of a diversified selection, of fixed income securities, including money market funds and instruments, corporate notes and bonds, government agency securities and other debt securities issued by financial institutions and other issuers with strong credit ratings. Changes in interest rates do not affect interest expense incurred on our convertible debentures because the debentures bear interest at fixed rates.

Our investment portfolio amounted to approximately $1,408.8 million at December 31, 2005. As of that date, we also had $173.3 million of floating rate obligations tied to the London Inter-Bank Offered Rate (LIBOR). We have a natural hedge against this exposure as a result of our portfolio holdings in floating rate fixed income securities tied to LIBOR. The analysis below describes the impact of changes in interest rates to us and is based on a net investment portfolio of $1,235.5 million.

The analysis assumes an immediate parallel increase or decrease in interest rates of 150-basis points and examines the impact to us over the next twelve months. An immediate increase in interest rates of 150-basis points results in interest income of $63.4 million over the subsequent 12-month period. Similarly, a 150-basis point decrease results in reported interest income of $38.8 million. Also, an immediate increase in interest rates of 150-basis points results in a decrease in the portfolio market value of $7.7 million. Fluctuations in the value of our investment securities caused by changes in interest rates (gains or losses on the carrying value) are recorded in other comprehensive income, and are realized only if we sell the underlying securities.

A larger than 150-basis point movement in short-term interest rates has occurred twice in the last ten years, a 100-150 basis point movement has occurred once in the last ten years, a 50-100 basis point movement has occurred in three of the last ten years, and a 0-50 basis point movement has occurred in four of the last ten years.

Equity Securities Risk

We have exposure to equity price risk because of our investments in equity securities. Typically, we obtain these securities through our collaboration agreements with other pharmaceutical and biotechnology partners. We classify a majority of these securities as available-for-sale and, consequently, record them on the balance sheet at fair value with unrealized gains or losses reported as a component of comprehensive income or loss. We periodically review the carrying values of these securities. We recognize impairment losses against earnings in the same period the loss was deemed to have occurred. Changes in share prices affect the value of our equity portfolio. To reduce this risk, we hedged a portion of our exposure through forward sales contracts. The forward sales contracts substantially offset any changes in value of the securities held and, in effect, neutralize the impact of market valuation shifts on the hedged portfolio. The notional amount of our forward sales contracts at December 31, 2005 was $12.9 million. The unrealized gain on outstanding forward sales contracts was $1.5 million at December 31, 2005. The notional amount of our forward sales contracts at December 31, 2004 was $41.5 million. The unrealized gain on outstanding forward sales contracts was $4.8 million at December 31, 2004. In the future, we may use additional hedging strategies in order to mitigate the potential adverse impact from changes in the market value of stock prices. We have no assurance that impairment losses will not have a material adverse impact on our future results of operations. We recorded charges of $1.3 million, $1.4 million, and $0.0 million in 2005, 2004, and 2003 respectively, to write down certain available-for-sale equity securities that we deemed to have been impaired. At December 31, 2005, if the market price of our equity investments, including warrants, decreased by 10%, the market value of the equity portfolio would decrease by $1.5 million.

Counterparty Risk

We manage the risk of counterparty default on our debt securities and derivative financial instruments through the use of credit standards, counterparty diversification and monitoring of counterparty financial condition. We execute debt securities and derivative financial transactions with financial institutions and other issuers with strong credit ratings, which reduce the risk of loss due to nonpayment or deterioration in credit rating.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

We incorporate the information required for this item by reference to the financial statements listed in Item 15(a) of Part IV of this Form 10-K.

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

Not applicable.

ITEM 9A. CONTROLS AND PROCEDURES

(a) Evaluation of disclosure controls and procedures As of the end of the period covered by this Annual Report, Chiron carried out an evaluation under the supervision and with the participation of Chiron s management, including Chiron s CEO and CFO, of the effectiveness of the design and operation of Chiron s disclosure controls and procedures. Based on that evaluation, Chiron s management, including the CEO and CFO, concluded that as of December 31, 2005 Chiron s disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms.

(b) Management s annual report on internal control over financial reporting

The management of Chiron Corporation is responsible for establishing and maintaining adequate internal control over financial reporting. Chiron s internal control system was designed to provide reasonable assurance to the Company s management and board of directors regarding the preparation and fair presentation of published financial statements.

The management of Chiron assessed the effectiveness of the Company s internal control over financial reporting as of December 31, 2005. In making its assessment of internal control over financial reporting management used the criteria issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control Integrated Framework.* Based on the assessment using those criteria, management concluded that, as of December 31, 2005, our internal control over financial reporting was effective.

Ernst & Young LLP, an independent registered public accounting firm that has audited our consolidated financial statements included herein, has issued an attestation report on our assessment of internal control over financial reporting.

(c) Report of the independent registered public accounting firm on internal control over financial reporting

The Board of Directors and Stockholders of Chiron Corporation

We have audited management s assessment, included in Management s annual report on internal control over financial reporting above, that Chiron Corporation 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 (the COSO criteria). Chiron Corporation 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 an opinion on management s assessment and an opinion on the effectiveness of the company s internal control over financial reporting based on our audit.

We conducted our audit 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. Our audit included 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 considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

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 (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) 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 (3) 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.

In our opinion, management s assessment that Chiron Corporation maintained effective internal control over financial reporting as of December 31, 2005, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, Chiron Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Chiron Corporation as of December 31, 2005 and 2004, and the related consolidated statements of operations, comprehensive income (loss), stockholders equity and cash flows for each of the three years in the period ended December 31, 2005 of Chiron Corporation and our report dated March 14, 2006 (except for Note 20, as to which the date is March 16, 2006) expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Palo Alto, California

March 14, 2006

(d) Changes in internal controls As of December 31, 2004 the Company s assessment of the effectiveness of its internal control over financial reporting identified three material weaknesses in the Company s internal control over financial reporting. During the fourth quarter of fiscal year 2005, and in connection with the preparation of our consolidated financial statements for the year ended December 31, 2005, we implemented additional controls and procedures relating to the annual tax provision process to address the material weakness that had been identified in 2004. Such additional controls and procedures included, among others:

- The implementation of new analytical tools in order to enhance the analysis and calculation of the tax provision and other tax accounts

- Additional training of personnel responsible for the tax provision process

As of December 31, 2005, the Company had remediated the controls that led to the prior year s material weaknesses, which pertained to both the design and operating effectiveness of controls relating to revenue recognition at our vaccines subsidiary in Germany, the annual income tax provision and the timely determination of the appropriate accrual for legal services.

Except as discussed above, there were no changes in the company s internal control over financial reporting during its most recently completed fiscal quarter that have materially affected or are reasonably likely to materially affect its internal control over financial reporting, as defined in Rule 13a-15(f) under the Exchange Act.

ITEM 9B. OTHER INFORMATION

Not applicable.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

We incorporate the information required for this item by reference to our definitive Proxy Statement for our 2006 Annual Meeting. We intend to file our Proxy Statement with the Securities and Exchange Commission within 120 days of December 31, 2005. See the sections entitled Election of Directors, Section 16(a) Beneficial Ownership Reporting Compliance and Corporate Governance Matters in the

Proxy Statement. For information on our executive officers, refer to the section entitled Executive Officers of the Registrant which appears at the end of Part I of this 10-K.

ITEM 11. EXECUTIVE COMPENSATION

We incorporate the information required for this item by reference to our Proxy Statement. See the sections entitled Compensation of Directors and Executive Compensation and Related Information in the Proxy Statement.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

We incorporate the stock ownership information required for this item by reference to our Proxy Statement. See the section entitled Stock Ownership in the Proxy Statement.

Equity Compensation Plan Information

The table below shows the securities authorized for issuance under Chiron s equity compensation plans in effect at December 31, 2005. Chiron does not maintain any equity compensation plans that have not been approved by its stockholders.

	(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights	(b) Weighted average exercise price of outstanding options, warrants and rights	(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders	27,775,631 (1)(2)(3)	$ 39.87	16,707,840 (4)
Equity compensation plans not approved by security holders			
Total	27,775,631		16,707,840

(1) Excludes purchase rights accruing under the Purchase Program component of the 2004 Stock Compensation Plan (the Stock Plan); the Stock Plan has a shareholder approved reserve of 79.2 million shares of which up to 6,400,000 shares may be issued under the Purchase Program. Under the Purchase Program as in effect on December 31, 2005, each eligible employee may purchase up to 2,700 shares of common stock during a 3 month offering period; shares are purchased during the offering period at quarterly intervals on the last business day of March, June, September and December each year; common stock will be purchased on the eligible employee s behalf at a purchase price equal to ninety percent (90%) of the fair market value per share of common stock on the purchase date; and the fair market value is equal to the average of the high and low selling prices of the common stock as reported on the Nasdaq National Market on the purchase date.

(2) Includes 839,705 shares reserved for issuance under outstanding share right awards issued under the Stock Plan. The outstanding share right awards will vest upon the completion of a designated service period or attainment of specified performance goals. As the award vests, shares will be issued to the holder with no cash payment to us required. The weighted average exercise price indicated in column (b) does not take the share right awards into account.

(3) Includes 56,386 shares subject to outstanding options granted in substitution of options held by employees of Pathogenesis Corporation at the time of its acquisition by Chiron in September 2000. The weighted average exercise price of these options is $31.38. At the time of the acquisition, Chiron granted substitute options for 207,293 shares with a weighted average exercise price of $30.12.

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(4) Consists of shares available for future issuance under the Stock Plan. As of December 31, 2005, 10,869,919 shares of our common stock were available for issuance under the Stock Plan. In accordance with the current terms of the Stock Plan, the number of shares of our common stock available for issuance under that plan automatically increases on the first trading day of January each calendar year by an amount equal to the lesser of (i) one percent (1.0%) of the number of Chiron Common Equivalent Shares outstanding as of the end of the preceding fiscal year or (ii) 3 million shares. Chiron Common Equivalent Shares are the total number of shares of common stock outstanding plus the total number of shares of common stock issuable upon conversion or exercise of outstanding warrants, options and convertible securities.

We incorporate the other information required for this item by reference to our Proxy Statement. See the section entitled Stock Ownership in the Proxy Statement.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

We incorporate the information required for this item by reference to our Proxy Statement. See the section entitled Certain Relationships and Related Transactions in the Proxy Statement.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

We incorporate the information required by this item by reference to our Proxy Statement. See section entitled Ratification of Appointment of Independent Auditors Independent Auditor Fee Information in the Proxy Statement.

Except for the information incorporated by references in Items 10, 11, 12, 13 and 14 of this Form 10-K, our definitive Proxy Statement is not deemed filed as part of this Form 10-K.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) The following documents are filed as part of this report:

1. Index to Consolidated Financial Statements

2. Index to Financial Statement Schedules

We omitted all other schedules because those schedules are not applicable, not required or because the required information is included in the Consolidated Financial Statements or accompanying notes.

(b) Exhibits. The Exhibits listed below are filed as part of this report.

Exhibit Number	Exhibit
2.01	Agreement and Plan of Merger, dated as of October 30, 2005, among Novartis Corporation, Novartis Biotech Partnership, Inc., Chiron and Novartis AG, incorporated by reference to Exhibit 2.01 of Chiron s current report on Form 8-K filed with the Commission on November 1, 2005.
3.01	Restated Certificate of Incorporation of Chiron, as filed with the Office of the Secretary of State of Delaware on August 17, 1987, incorporated by reference to Exhibit 3.01 of Chiron s report on Form 10-K for fiscal year 1996.
3.02	Certificate of Amendment of Restated Certificate of Incorporation of Chiron, as filed with the Office of the Secretary of State of Delaware on December 12, 1991, incorporated by reference to Exhibit 3.02 of the Chiron s report on Form 10-K for fiscal year 1996.
3.03	Certificate of Amendment of Restated Certificate of Incorporation of Chiron, as filed with the Office of the Secretary of St1ate of Delaware on May 22, 1996, incorporated by reference to Exhibit 3.04 of Chiron s report on Form 10-Q for the period ended June 30, 1996.
3.04	Bylaws of Chiron, as amended and restated, incorporated by reference to Exhibit 99.1 of Chiron s current report on Form 8-K filed with the Commission on March 10, 2005.

4.01	Indenture between Chiron and State Street Bank and Trust Company, dated as of June 12, 2001, incorporated by reference to Exhibit 4.01 of Chiron s report on Form 10-Q for the period ended June 30, 2001.
4.02	Registration Rights Agreement between Chiron and Merrill Lynch & Co., Inc., and Merrill Lynch, Pierce, Fenner & Smith, Incorporated, incorporated by reference to Exhibit 4.02 of Chiron s report on Form 10-Q for the period ended June 30, 2001.
4.03	Form of Liquid Yield Option Note due 2031 (Zero Coupon Senior) (included as exhibits A-1 and A-2 to the Indenture filed as Exhibit 4.01 to Chiron s report on Form 10-Q for the period ended June 30, 2001), incorporated by reference to Exhibit 4.03 of Chiron s report on Form 10-Q for the period ended June 30, 2001.
4.04	Indenture between Chiron and U.S. Bank National Association, as trustee, dated as of July 30, 2003, incorporated by reference to Exhibit 4.1 of Chiron s registration statement on Form S-3 filed with the Commission on September 23, 2003.
4.05	Registration Rights Agreement dated as of July 30, 2003, between Chiron and Morgan Stanley & Co., Goldman, Sachs & Co., Banc of America Securities LLC and BNP Paribas Securities Corp., incorporated by reference to Exhibit 4.3 of Chiron s registration statement on Form S-3 filed with the Commission on September 23, 2003.
4.06	Form of Convertible Debentures (included in Exhibit 4.04), incorporated by reference to Exhibit 4.2 of Chiron s registration statement on Form S-3 filed with the Commission on September 23, 2003.
4.07	Indenture between Chiron and U.S. Bank National Association, as trustee, dated as of June 22, 2004, incorporated by reference to Exhibit 4.07 of Chiron s report on Form 10-Q for the period ended June 30, 2004.
4.08	Registration Rights Agreement dated as of June 22, 2004, between Chiron, Credit Suisse First Boston, LLC and Morgan Stanley & Co., Goldman, Sachs & Co., Incorporated, incorporated by reference to Exhibit 4.08 of Chiron s report on Form 10-Q for the period ended June 30, 2004.
4.09	Specimen of Convertible Debentures (included as Exhibit A to the Indenture referenced as Exhibit 4.07 of Chiron s report on Form 10-Q for June 30, 2004) issued on June 22, 2004, incorporated by reference to Exhibit 4.09 of Chiron s report on Form 10-Q for the period ended June 30, 2004.
4.10	Reserved
10.001	Purchase Agreement between BNP Leasing Corporation and Chiron, dated June 28, 1996, incorporated by reference to Exhibit 10.90 of Chiron s report on Form 10-Q for the period ended June 30, 1996.
10.002	Lease Agreement between BNP Leasing Corporation and Chiron, dated June 28, 1996, incorporated by reference to Exhibit 10.91 of Chiron s report on Form 10-Q for the period ended June 30, 1996.
10.003	Ground Lease between BNP Leasing Corporation and Chiron, dated June 28, 1996, incorporated by reference to Exhibit 10.92 of Chiron s report on Form 10-Q for the period ended June 30, 1996.

10.004	Second Amendment between BNP Paribas Leasing Corporation, a Delaware corporation (as successor in interest to BNP Leasing Corporation) (BNPLC), and Chiron, dated July 1, 2003, incorporated by reference to Exhibit 10.004 of Chiron s report on Form 10-Q for the period ended June 30, 2003.
*10.005	Agreement for Lease dated effective December 23, 2003, between Intercity Pharma Limited, as developer, and Evans Vaccines Limited, as tenant, incorporated by reference to Exhibit 10.005 of Chiron s report on Form 10-K for fiscal year 2003.
10.006	Through 10.101 Reserved
10.102	Amended and Restated Revolving Credit Agreement, dated as of August 13, 2002, by and between Chiron and Bank of America, N.A., and exhibits thereto, incorporated by reference to Exhibit 10.102 of Chiron s report on Form 10-Q for the period ended September 30, 2002.
10.103	Reserved
10.104	Stock Purchase and Warrant Agreement dated May 9, 1989, between Cetus Corporation and Hoffmann-La Roche Inc. (initially filed as Exhibit 10.36 of Chiron s report on Form 10-Q for the period ended September 30, 1994), incorporated by reference to Exhibit 10.104 of Chiron s report on Form 10-Q for the period ended June 30, 1999.
10.105	Letter Agreement, dated as of December 12, 1991, relating to Stock Purchase and Warrant Agreement between Chiron and Hoffmann-La Roche Inc., incorporated by reference to Exhibit 10.51 of Chiron s report on Form 10-K for fiscal year 1996.
10.106	Through 10.200Reserved
*10.201	Agreement between Chiron and Ortho Diagnostic Systems, Inc., a New Jersey corporation, dated August 17, 1989, and Amendment to Collaboration Agreement between Ortho Diagnostic Systems, Inc. and Chiron, dated December 22, 1989 (with certain confidential information deleted), (initially filed as Exhibit 10.29 to Chiron s report on Form 10-K for fiscal year 1989, and refiled as Exhibit 10.14 of Chiron s report on Form 10-Q for the period ended September 30, 1994), incorporated by reference to Exhibit 10.201 of Chiron s report on Form 10-Q for the period ended March 31, 1999.
*10.202	License and Supply Agreement between Ortho Diagnostic Systems, Inc., a New Jersey corporation, Chiron and Abbott Laboratories, an Illinois corporation, dated August 17, 1989 (initially filed as Exhibit 10.31 to Chiron s report on Form 10-K for fiscal year 1989, and refiled as Exhibit 10.15 of Chiron s report on Form 10-Q for the period ended June 30, 1994), incorporated by reference to Exhibit 10.202 of Chiron s report on Form 10-Q for the period ended March 31, 1999.
*10.203	Regulatory Filing, Development and Supply Agreement between Chiron, Cetus Oncology Corporation, a wholly-owned subsidiary of Chiron, and Schering AG, a German company, dated as of May 10, 1993 (initially filed as Exhibit 10.50 to Chiron s report on Form 10-Q for the period ended September 30, 1993), incorporated by reference to Exhibit 10.203 of Chiron s report on Form 10-K for fiscal year 1998.
*10.204	Letter Agreement dated December 30, 1993 by and between Chiron and Schering AG, a German company (initially filed as Exhibit 10.51 to Chiron s report on Form 10-K for fiscal year 1993), incorporated by reference to Exhibit 10.204 of Chiron s report on Form 10-K for fiscal year 1998.

*10.205	Amendment Agreement (HDS Fees and Deeply Discounted Vials) dated as of September 23, 1997 between Chiron and Schering Aktiengesellschaft, incorporated by reference to Exhibit 10.205 of Chiron s report on Form 10-K for fiscal year 1997.
*10.206	Reserved
*10.207	Letter Agreement dated as of December 4, 1997, between Chiron and Ortho Pharmaceutical Corporation and Ortho Biotech, Inc., incorporated by reference to Exhibit 10.207 of Chiron s report on Form 10-K for fiscal year 1997.
*10.208	Reserved
*10.209	Second Amendment Agreement dated as of June 15, 2001, between Chiron and Schering Aktiengesellschaft, incorporated by reference to Exhibit 10.209 of Chiron s report on Form 10-Q for the period ended June 30, 2001.
10.210	Reserved
*10.211	Side Letter Agreement dated as of December 20, 2002, between Chiron and Schering Berlin, Inc., incorporated by reference to Exhibit 10.211 of Chiron s report on Form 10-Q for the period ended March 31, 2003, incorporated by reference to Exhibit 10.211 of Chiron s report on Form 10-Q for the period ended June 30, 2003.
*10.212	Contract Manufacturing Agreement dated as of June 12, 2003, between Chiron S.r.l., Chiron Behring GmbH & Co., and SynCo Bio Partners B.V., incorporated by reference to Exhibit 10.212 of Chiron s report on Form 10-Q for the period ended June 30, 2003.
*10.213	FDA Compliance Agreement dated as of June 12, 2003, between Chiron S.r.l, Chiron Behring GmbH & Co and SynCo Bio Partners B.V., incorporated by reference to Exhibit 10.213 of Chiron s report on Form 10-Q for the period ended June 30, 2003.
10.214	Through 10.300 Reserved
*10.301	Settlement Agreement on Purified IL-2, made as of April 14, 1995, by and between Cetus Oncology Corporation, dba Chiron Therapeutics, a Delaware corporation, and Takeda Chemical Industries, Ltd., a Japanese corporation, incorporated by reference to Exhibit 10.74 of the Chiron s report on Form 10-Q for the period ended July 2, 1995.
*10.302	Agreement, effective as of December 21, 1988, by and between Hoffmann-La Roche Inc., a New Jersey corporation, and Cetus Corporation, incorporated by reference to Exhibit 10.70 of Chiron s report on Form 10-Q for the period ended April 2, 1995.
*10.303	Agreement, effective as of December 21, 1988, by and among F. Hoffmann-La Roche Ltd., a Swiss corporation, Cetus Corporation, and EuroCetus International, B.V., a Netherlands Antilles corporation, incorporated by reference to Exhibit 10.71 of Chiron s report on Form 10-Q for the period ended April 2, 1995.
*10.304	License Agreement made and entered into December 1, 1987, by and between Sloan Kettering Institute for Cancer Research, a not-for-profit New York corporation, and Cetus Corporation, incorporated by reference to Exhibit 10.75 of Chiron s report on Form 10-Q for the period ended July 2, 1995.
*10.305	Cross-License Agreement dated as of November 30, 1998, between Chiron and Chiron Diagnostics Corporation, incorporated by reference to Exhibit 10.311 of Chiron s current report on Form 8-K filed with the Commission on December 15, 1998.

*10.306	HCV Probe License and Option Agreement dated September 26, 1999, between Abbott Laboratories, an Illinois corporation, and Chiron, incorporated by reference to Exhibit 10.306 of Chiron s report on Form 10-Q for the period ended September 30, 1999.
*10.307	HCV Probe License Agreement dated October 10, 2000, between Chiron, F. Hoffmann-La Roche Ltd. and Roche Molecular Systems, Inc., incorporated by reference to Exhibit 10.307 of Chiron s report on Form 10-Q for the period ended September 30, 2000.
*10.308	HIV Probe License Agreement dated October 10, 2000, between Chiron, F. Hoffmann-La Roche Ltd. and Roche Molecular Systems, Inc., incorporated by reference to Exhibit 10.308 of Chiron s report on Form 10-Q for the period ended September 30, 2000.
*10.309	Blood Screening HCV/HIV Probe License Agreement dated October 10, 2000, between Chiron, F. Hoffmann-La Roche Ltd. and Roche Molecular Systems, Inc., incorporated by reference to Exhibit 10.309 of Chiron s report on Form 10-Q for the period ended September 30, 2000.
10.310	Reserved
*10.311	Agreement with Gen-Probe Incorporated dated June 11, 1998, incorporated by reference to Exhibit 10.311 of Chiron s Form 10-K for fiscal year 2000. (We have omitted certain information from the Agreement relating to rights and obligations assigned by Chiron to unrelated third party subsequent to the execution of Agreement. We have identified the omitted information by the following statement: Provision Assigned.)
*10.312	Addendum to Agreement with Gen-Probe Incorporated dated June 11, 1998, incorporated by reference to Exhibit 10.312 of Chiron s Form 10-K for fiscal year 2000. (We have omitted certain information from the Agreement relating to rights and obligations assigned by Chiron to unrelated third party subsequent to the execution of Agreement. We have identified the omitted information by the following statement: Provision Assigned.)
*10.313	Amendment to Agreement with Gen-Probe Incorporated dated December 7, 1999, incorporated by reference to Exhibit 10.313 of Chiron s Form 10-K for fiscal year 2000. (We have omitted certain information from the Agreement relating to rights and obligations assigned by Chiron to unrelated third party subsequent to the execution of Agreement. We have identified the omitted information by the following statement: Provision Assigned.)
*10.314	Amendment No. 2 to Agreement with Gen-Probe Incorporated dated February 1, 2000, incorporated by reference to Exhibit 10.314 of Chiron s report on Form 10-K for fiscal year 2002. (We have omitted certain information from the Agreement relating to rights and obligations assigned by Chiron to unrelated third party subsequent to the execution of Agreement. We have identified the omitted information by the following statement: Provision Assigned.)
*10.315	Blood Screening HCV Probe License Agreement dated effective as of January 1, 2001, between Chiron, F. Hoffmann-La Roche Ltd. and Roche Molecular Systems, Inc., incorporated by reference to Exhibit 10.315 of Chiron s report on Form 10-Q for the period ended June 30, 2001.
*10.316	Blood Screening HIV Probe License Agreement dated effective as of January 1, 2001, between Chiron, F. Hoffmann-La Roche Ltd. and Roche Molecular Systems, Inc., incorporated by reference to Exhibit 10.316 of Chiron s report on Form 10-Q for the period ended June 30, 2001.

*10.317	Association Agreement Regarding the Sale and Servicing of Blood Screening Products, dated as of May 1, 2002, between America s Blood Centers and Chiron, and Form of Member Supplement, incorporated by reference to Exhibit 10.317 of Chiron s report on Form 10-Q for the period ended June 30, 2002.
*10.318	Amendment No. 3 to Agreement with Gen-Probe Incorporated entered into effective April 1, 2002, incorporated by reference to Exhibit 10.318 of Chiron s report on Form 10-Q for the period ended September 30, 2002.
*10.319	Sale and Servicing Agreement made effective as of August 1, 2002, between The American National Red Cross and Chiron, incorporated by reference to Exhibit 10.319 of Chiron s report on Form 10-K for fiscal 2002.
*10.320	Amendment No. 4 to Agreement with Gen-Probe Incorporated entered into effective March 5, 2003, incorporated by reference to Exhibit 10.320 of Chiron s report on Form 10-Q for the period ended March 31, 2003.
*10.321	Blood Screening HCV Probe License Agreement-European Union dated effective as of July 1, 2003, between Chiron, F. Hoffmann-La Roche Ltd., and Roche Molecular Systems, Inc., incorporated by reference to Exhibit 10.321 of Chiron s report on Form 10-Q for the period ended June 30, 2003.
*10.322	Blood Screening HIV Probe License Agreement-European Union dated effective as of July 1, 2003, between Chiron, F. Hoffmann-La Roche Ltd., and Roche Molecular Systems, Inc., incorporated by reference to Exhibit 10.322 of Chiron s report on Form 10-Q for the period ended June 30, 2003.
*10.323	HCV Probe License and Option Agreement-European Union dated effective as of July 1, 2003, between Chiron, F. Hoffmann-La Roche Ltd., and Roche Molecular Systems, Inc., incorporated by reference to Exhibit 10.323 of Chiron s report on Form 10-Q for the period ended June 30, 2003.
*10.324	HIV Probe License and Option Agreement-European Union dated effective as of July 1, 2003, between Chiron, F. Hoffmann-La Roche Ltd., and Roche Molecular Systems, Inc., incorporated by reference to Exhibit 10.324 of Chiron s report on Form 10-Q for the period ended June 30, 2003.
*10.325	Agreement, dated as of July 1, 2003, between The American National Red Cross and Chiron, incorporated by reference to Exhibit 10.325 of Chiron s report on Form 10-Q for the period ended September 30, 2003.
*10.326	WNV Association Agreement, dated as of July 1, 2003, between America s Blood Centers and Chiron, and Form of Member Supplement, incorporated by reference to Exhibit 10.326 of Chiron s report on Form 10-Q for the period ended September 30, 2003.
*10.327	Amendment No. 5 to Agreement with Gen-Probe Incorporated entered into effective as of January 1, 2004, incorporated by reference to Exhibit 10.327 of Chiron s report on Form 10-K for fiscal year 2003.
*10.328	Future Blood Screening Assay West Nile Virus Addendum dated October 21, 2003, amending Agreement entered into as of June 11, 1998 by and between Gen-Probe Incorporated and Chiron, incorporated by reference to Exhibit 10.328 of Chiron s report on Form 10-K for fiscal year 2003.

*10.329	Future Blood Screening Assay ULTRIO Addendum dated March 24, 2003, amending Agreement entered into as of June 11, 1998 by and between Gen-Probe Incorporated and Chiron, incorporated by reference to Exhibit 10.329 of Chiron s report on Form 10-K for fiscal year 2003.
*10.330	Term Sheet effective as of September 3, 2004 with Roche Diagnostics GmbH, incorporated by reference to Exhibit 10.330 of Amendment No. 1 to Chiron s report on Form 10-Q/A for the period ended September 30, 2004.
*10.331	Modified Blood Screening Instrument eSAS 2 Addendum Amending the Agreement entered into as of June 11, 1998, between Chiron and Gen-Probe, Incorporated, effective as of January 1, 2002, incorporated by reference to Exhibit 10.331 of Chiron s report on Form 10-Q for the period ended March 31, 2005.
*10.332	Amendment No. 6 to Agreement with Gen-Probe Incorporated, entered into effective as of January 1, 2004, incorporated by reference to Exhibit 10.332 of Chiron s report on Form 10-Q for the period ended March 31, 2005.
10.333	Amendment No. 7 to Agreement with Gen-Probe Incorporated dated May 20, 2005.
10.334	Amendment No. 8 to Agreement with Gen-Probe Incorporated, entered into effective as of February 8, 2006.
10.335	Through 10.400 Reserved
10.401	Stock Purchase Agreement, dated as of October 21, 1997, between Bausch & Lomb Incorporated and Chiron, incorporated by reference to Exhibit 99.1 of Chiron s current report on Form 8-K filed with the Commission on January 13, 1998.
*10.402	Stock Purchase Agreement, dated as of September 17, 1998, among Bayer Corporation, Chiron and Chiron Diagnostics Corporation, and Exhibits thereto, incorporated by reference to Exhibit 10.402 of Chiron s report on Form 10-Q for the period ended September 27, 1998.
*10.403	Asset Transfer Agreement dated November 30, 1998, among Chiron, Chiron Diagnostics Corporation and Bayer Corporation, incorporated by reference to Exhibit 10.403 of Chiron s current report on Form 8-K filed with the Commission on December 15, 1998.
10.404	Agreement and Plan of Merger, dated as of January 6, 2002, among Chiron, Manon Acquisition Corp. and Matrix Pharmaceutical, Inc., incorporated by reference to Exhibit (d)(1) of Chiron s Schedule TO-T No. 00542277, filed with the Commission on January 14, 2002.
10.405	Through 10.500 Reserved
**10.501	Chiron 2004 Stock Compensation Plan, incorporated by reference to Exhibit 10.501 of Chiron s report on Form 10-Q for the period ended June 30, 2004.
**10.502	Form of Stock Option Agreement, and Addendum to Stock Option Agreement (Executives), Chiron 1991 Stock Option Plan, as amended, incorporated by reference to Exhibit 10.502 of Chiron s report on Form 10-K for fiscal year 2001.
**10.503	Forms of Stock Option Agreements, Chiron 1991 Stock Option Plan, as amended, for Non-Employee Directors of Chiron, incorporated by reference to Exhibit 10.503 of Chiron s report on Form 10-Q for the period ended June 30, 2002.

**10.504	Form of Automatic Share Right Agreement for Executive Officers, Chiron 1991 Stock Option Plan, as amended, incorporated by reference to Exhibit 10.504 of Chiron s report on Form 10-K for fiscal year 2001.
**10.505	Form of Amendment Letter to Automatic Share Rights Letter Agreement for Non-Employee Directors of Chiron, Chiron 1991 Stock Option Plan, as amended, incorporated by reference to Exhibit 10.505 of Chiron s report on Form 10-Q for the period ended June 30, 2002.
**10.506	Form of Amendment Letter to Automatic Stock Option Agreement for Non-Employee Directors of Chiron, Chiron 1991 Stock Option Plan, as amended, incorporated by reference to Exhibit 10.506 of Chiron s report on Form 10-Q for the period ended June 30, 2002.*
**10.507	Chiron Executive Officer Severance Plan.
**10.508	Form of Performance Share Rights Agreement (Executive Officers), incorporated by reference to Exhibit 10.508 of Chiron s report on Form 10-Q for the period ended June 30, 2004.
**10.509	Description of Chiron s 2005 Executive Officers Variable Compensation Program.
**10.510	Form of Deferred Share Units Grant for Executive Officers, Chiron 2004 Stock Compensation Plan.
10.511	Audit Committee Charter, as amended and restated as of September 14, 2005, incorporated by reference to Exhibit 10.511 of Chiron s report on Form 10-Q for the period ended September 30, 2005.
**10.512	Change-in-Control Severance Plan (Tier II Executive Committee Members).
**10.513	Form of Performance Stock Option Agreement for Executive Officers, Chiron 1991 Stock Option Plan, as amended and restated, incorporated by reference to Exhibit 10.513 of Chiron s report on Form 10-K for fiscal year 2001.
**10.514	Form of Amendment Letter to Share Rights Letter Agreement for Executive Officers, Chiron 1991 Stock Option Plan, as amended and restated, incorporated by reference to Exhibit 10.514 of Chiron s report on Form 10-K for fiscal year 2001.
**10.515	Form of Amendment Letter to Stock Option Agreement (Special Executive Form) for Executive Officers, Chiron 1991 Stock Option Plan, as amended and restated, incorporated by reference to Exhibit 10.515 of Chiron s report on Form 10-K for fiscal year 2001.
10.516	Compensation Committee Charter, incorporated by reference to Exhibit 10.319 of Chiron s report on Form 10-K for fiscal year 2002.
**10.517	Chiron Supplemental Executive Retirement Plan, as amended and restated effective March 1, 2003, incorporated by reference to Exhibit 10.517 of Chiron s report on Form 10-Q for the period ended March 31, 2003.
10.518	Nominating and Corporate Governance Committee Charter, incorporated by reference to Exhibit 10. 518 of Chiron s report on Form 10-Q for the period ended June 30, 2003.
10.519	Corporate Governance Guidelines, as amended and restated, incorporated by reference to Exhibit 10. 519 of Chiron s report on Form 10-Q for the period ended September 30, 2004.
10.520	Finance Committee Charter, incorporated by reference to Exhibit 10.520 of Chiron s report on Form 10-Q for the period ended June 30, 2004.

**10.521	Chiron Supplemental Retirement Plan, incorporated by reference to Exhibit 4.1 to Chiron s Registration Statement on Form S-8 (Reg. No. 333-121126), filed with the Commission on December 9, 2004.
**10.522	Amendment No. 1 to Chiron 2004 Stock Compensation Plan, effective December 1, 2005.
10.523	Through 10.600 Reserved
10.601	Indemnification Agreement between Chiron and Dr. William J. Rutter, dated as of February 12, 1987 (which form of agreement is used for each member of Chiron s Board of Directors) (initially filed as Exhibit 10.21 of Chiron s report on Form 10-Q for the quarterly period ended September 30, 1994), incorporated by reference to Exhibit 10.601 of Chiron s report on Form 10-Q for the quarterly period ended June 30, 1999.
**10.602	Change-in-Control Severance Plan (Tier I Chief Executive Officer).
**10.603	Letter Agreement dated September 26, 1990, between Chiron and William G. Green (initially filed as Exhibit 10.41 of Chiron s report on Form 10-K for fiscal year 1992), incorporated by reference to Exhibit 10.603 of Chiron s report on Form 10-K for fiscal year 1998.
10.604	Through 10.610 Reserved
*10.611	Letter Agreement dated January 17, 2001, with an effective date of January 22, 2001, and Addendum dated January 11, 2001, between Gene W. Walther and Chiron.
10.612	Reserved
**10.613	Letter Agreement dated January 25, 1999, between Chiron and David V. Smith, incorporated by reference to Exhibit 10.613 of Chiron s report on Form 10-K for fiscal year 2004.
**10.614	Compromise Agreement dated February 18, 2005, between John A. Lambert and Chiron, incorporated by reference to Exhibit 10.614 of Chiron s report on Form 10-Q for the period ended March 31, 2005.
**10.615	Letter Agreement dated February 28, 2005 (agreed to on March 4, 2005), between Jack Goldstein and Chiron, incorporated by reference to Exhibit 10.615 of Chiron s report on Form 10-Q for the period ended March 31, 2005.
10.616	Through 10.619 Reserved
**10.620	Letter Agreement dated August 1, 2001, between Chiron and Craig A. Wheeler, incorporated by reference to Exhibit 10.620 of Chiron s report on Form 10-K for fiscal year 2002.
**10.621	Letter Agreement dated March 19, 2003, between Chiron and Howard H. Pien, incorporated by reference to Exhibit 10.621 of Chiron s report on Form 10-Q for the period ended March 31, 2003.
**10.622	Letter Agreement dated February 16, 2001, between Chiron and John A. Lambert, incorporated by reference to Exhibit 10.622 of Chiron s report on Form 10-Q for the period ended March 31, 2003.
**10.623	Letter Agreement dated July 1, 2003, between Chiron and John A. Lambert, incorporated by reference to Exhibit 10.623 of Chiron s report on Form 10-K for fiscal year 2003.

**10.624	Letter Agreement dated August 12, 2003, between Chiron and Craig A. Wheeler, incorporated by reference to Exhibit 10.624 of Chiron s report on Form 10-Q for the period ended September 30, 2003.
**10.625	Letter Agreement dated January 26, 2004, between Chiron and John A. Lambert, incorporated by reference to Exhibit 10.625 of Chiron s report on Form 10-K for fiscal year 2003.
**10.626	Letter Agreement dated July 7, 2004, between Ursula B. Bartels and Chiron, incorporated by reference to Exhibit 10.626 of Chiron s report on Form 10-Q for the period ended September 30, 2004.
**10.627	Supplemental Pension Agreement dated as of July 20, 2004, between Chiron and William G. Green, incorporated by reference to Exhibit 10.627 of Chiron s report on Form 10-Q for the period ended September 30, 2004.
**10.628	Letter agreement dated October 20, 2005, between Howard H. Pien and Chiron, incorporated by reference to Exhibit 99.1 of Chiron s current report on Form 8-K filed with the Commission on October 26, 2005.
10.629	Through 10.700 Reserved
10.701	Investment Agreement dated as of November 20, 1994 among Ciba-Geigy Limited, Ciba-Geigy Corporation, Ciba Biotech Partnership, Inc. and Chiron Corporation (initially filed as Exhibit 10.54 of the Chiron s current report on Form 8-K dated November 20, 1994), incorporated by reference to Exhibit 10.701 of Chiron s report on Form 10-Q for the period ended June 30, 1999.
10.702	Governance Agreement dated as of November 20, 1994 among Ciba-Geigy Limited, Ciba-Geigy Corporation and Chiron Corporation (initially filed as Exhibit 10.55 of Chiron s current report on Form 8-K dated November 20, 1994), incorporated by reference to Exhibit 10.702 of Chiron s report on Form 10-Q for the period ended June 30, 1999.
10.703	Subscription Agreement dated as of November 20, 1994 among Ciba-Geigy Limited, Ciba-Geigy Corporation, Ciba Biotech Partnership, Inc. and Chiron Corporation (initially filed as Exhibit 10.56 of Chiron s current report on Form 8-K dated November 20, 1994), incorporated by reference to Exhibit 10.703 of Chiron s report on Form 10-Q for the period ended June 30, 1999.
10.704	Cooperation and Collaboration Agreement dated as of November 20, 1994, between Ciba-Geigy Limited and Chiron Corporation (initially filed as Exhibit 10.57 of Chiron s current report on Form 8-K dated November 20, 1994), incorporated by reference to Exhibit 10.704 of Chiron s report on Form 10-Q for the period ended June 30, 1999.
10.705	Registration Rights Agreement dated as of November 20, 1994 between Ciba Biotech Partnership, Inc. and Chiron Corporation (initially filed as Exhibit 10.58 of Chiron s current report on Form 8-K dated November 20, 1994), incorporated by reference to Exhibit 10.705 of Chiron s report on Form 10-Q for the period ended June 30, 1999.

10.706	Market Price Option Agreement dated as of November 20, 1994 among Ciba-Geigy Limited, Ciba-Geigy Corporation, Ciba Biotech Partnership, Inc. and Chiron Corporation (initially filed as Exhibit 10.59 of Chiron s current report on Form 8-K dated November 20, 1994), incorporated by reference to Exhibit 10.706 of Chiron s report on Form 10-Q for the period ended June 30, 1999.
10.707	Amendment dated as of January 3, 1995 among Ciba-Geigy Limited, Ciba-Geigy Corporation, Ciba Biotech Partnership, Inc. and Chiron Corporation (initially filed as Exhibit 10.60 of Chiron s current report on Form 8-K dated January 4, 1995), incorporated by reference to Exhibit 10.707 of Chiron s report on Form 10-Q for the period ended September 30, 1999.
10.708	Supplemental Agreement dated as of January 3, 1995 among Ciba-Geigy Limited, Ciba-Geigy Corporation, Ciba Biotech Partnership, Inc. and Chiron Corporation (initially filed as Exhibit 10.61 of Chiron s current report on Form 8-K dated January 4, 1995), incorporated by reference to Exhibit 10.708 of Chiron s report on Form 10-Q for the period ended September 30, 1999.
**10.709	Amendment with Respect to Employee Stock Option Arrangements dated as of January 3, 1995 among Ciba-Geigy Limited, Ciba-Geigy Corporation, Ciba Biotech Partnership, Inc. and Chiron Corporation, (initially filed as Exhibit 10.62 of Chiron s current report on Form 8-K dated January 4, 1995), incorporated by reference to Exhibit 10.709 of Chiron s report on Form 10-Q for the period ended September 30, 1999.
10.710	Agreement, dated November 27, 1996, between Ciba-Geigy Limited and Chiron, incorporated by reference to Exhibit 10.92 of Chiron s current report on Form 8-K filed with the Commission on December 17, 1996.
10.711	Amendment dated March 26, 1997, to Agreement dated November 27, 1996, between Novartis Pharma AG and Chiron, incorporated by reference to Exhibit 10.44 of Chiron s report on Form 10-Q for the period ended March 30, 1997.
10.712	Letter Agreement dated December 19, 1997, between Novartis Pharma AG and Chiron, incorporated by reference to Exhibit 10.712 of Chiron s report on Form 10-K for fiscal year 1997.
*10.713	Letter Agreement dated December 24, 1997, between Novartis Corporation and Chiron, incorporated by reference to Exhibit 10.713 of Chiron s report on Form 10-K for fiscal year 1997.
10.714	Letter Agreement, dated May 6, 1996, as to consent to assignment of contracts to Novartis Limited, among the Registrant, Ciba-Geigy Limited, Ciba-Geigy Corporation and Ciba Biotech Partnership, Inc., incorporated by reference to Exhibit 10.43 of Chiron s report on Form 10-K for fiscal year 1996.
**10.715	Letter Agreement, dated December 19, 1996, regarding compensation paid by Chiron for director services performed by employees of Ciba-Geigy Limited, incorporated by reference to Exhibit 10.44 of Chiron s report on Form 10-K for fiscal year 1996.
*10.716	Letter Agreement dated September 30, 1999, between Novartis Corporation and Chiron, incorporated by reference to Exhibit 10.716 of Chiron s report on Form 10-Q for the period ended September 30, 1999.

*10.717	Chiron Funding L.L.C. Limited Liability Company Agreement, entered into and effective as of December 28, 1995, among Chiron, Chiron Biocine Company and Biocine S.p.A. and Ciba-Geigy Corporation, incorporated by reference to Exhibit 10.80 of Chiron s report on Form 10-K for fiscal year 1995.
*10.718	Agreement between Ciba-Geigy Limited and Chiron made November 15, 1995, incorporated by reference to Exhibit 10.81 of Chiron s report on Form 10-K for fiscal year 1995.
10.719	Reimbursement Agreement dated as of March 24, 1995, between Ciba-Geigy Limited, a Swiss corporation, and Chiron, incorporated by reference to Exhibit 10.76 of Chiron s report on Form 10-Q for the period ended July 2, 1995.
10.719.1	Reimbursement Agreement dated as of May 20, 1996, between Ciba-Geigy Limited, a Swiss corporation, and Chiron, incorporated by reference to Exhibit 10.95 of Chiron s report on Form 10-Q for the period ended June 30, 1996.
10.720	Reimbursement Agreement, dated as of June 28, 1996, between Ciba-Geigy Limited, a Swiss corporation, and Chiron, incorporated by reference to Exhibit 10.94 of Chiron s report on Form 10-Q for the period ended June 30, 1996.
10.721	Reimbursement Agreement, dated as of July 12, 1996, between Ciba-Geigy Limited, a Swiss corporation, and Chiron, incorporated by reference to Exhibit 10.93 of Chiron s report on Form 10-Q for the period ended June 30, 1996.
**10.722	Letter Agreement dated December 31, 1999 between Novartis Corporation and Chiron, incorporated by reference to Exhibit 10.44 of Chiron s report on Form 10-K for fiscal year 1999.
10.723	Letter Agreement dated December 7, 2000, between Novartis Corporation and Chiron, incorporated by reference to Exhibit 10.723 of Chiron s report on Form 10-K for fiscal year 2000.
10.724	Amendment dated May 18, 2001 to Governance Agreement dated as of November 20, 1994, among Chiron and Novartis AG as successor-in-interest to Ciba-Geigy Limited, incorporated by reference to Exhibit 10.724 of Chiron s report on Form 10-K for fiscal year 2002.
10.725	