

APPLERA CORP  
Form 10-Q  
November 12, 2003  
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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

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**FORM 10-Q**

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

**For the quarterly period ended September 30, 2003**

OR

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

Commission file number: **1-4389**

**APPLERA CORPORATION**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**

(State or Other Jurisdiction of  
Incorporation or Organization)

**06-1534213**

(I.R.S. Employer  
Identification No.)

**301 Merritt 7, Norwalk, Connecticut**

(Address of Principal Executive Offices)

**06851-1070**

(Zip Code)

**(203) 840-2000**

(Registrant's Telephone Number, Including Area Code)

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

No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes

No

As of the close of business on November 5, 2003, there were 208,026,968 shares of Applera Corporation-Applied Biosystems Group Common Stock and 72,555,532 shares of Applera Corporation-Celera Genomics Group Common Stock outstanding.

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**APPLERA CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(unaudited)  
(Dollar amounts in thousands except per share amounts)

	Three Months Ended September 30,	
	2002	2003
<b>Net Revenues</b>	\$ 417,333	\$ <b>405,037</b>
Cost of sales	194,894	<b>190,478</b>
<b>Gross Margin</b>	222,439	<b>214,559</b>
Selling, general and administrative	108,101	<b>107,357</b>
Research, development and engineering	103,291	<b>92,412</b>
Amortization of intangible assets	2,700	<b>725</b>
<b>Operating Income</b>	8,347	<b>14,065</b>
Gain on investments, net		<b>545</b>
Interest expense	(210)	<b>(136)</b>
Interest income	8,589	<b>6,206</b>
Other income (expense), net	(2,115)	<b>(986)</b>
<b>Income before Income Taxes</b>	14,611	<b>19,694</b>
Provision for income taxes	2,546	<b>3,682</b>
<b>Income from Continuing Operations</b>	12,065	<b>16,012</b>
Loss from discontinued operations, net of income taxes	(16,400)	
<b>Net Income (Loss)</b>	\$ (4,335)	\$ <b>16,012</b>
<b>Applied Biosystems Group (see Note 3)</b>		
<b>Income from Continuing Operations</b>	\$ 34,222	\$ <b>33,378</b>
Basic and diluted per share	\$ 0.16	\$ <b>0.16</b>
<b>Loss from Discontinued Operations</b>	\$ (16,400)	\$ □
Basic and diluted per share	\$ (0.08)	\$ □
<b>Net Income</b>	\$ 17,822	\$ <b>33,378</b>
Basic and diluted per share	\$ 0.08	\$ <b>0.16</b>
<b>Dividends per share</b>	\$ 0.0425	\$ <b>0.0425</b>

**Celera Genomics Group (see Note 3)**

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<b>Net Loss</b>	\$	(19,649)	\$	<b>(16,286)</b>
Basic and diluted per share	\$	(0.28)	\$	<b>(0.23)</b>

See accompanying notes to the Applera Corporation unaudited condensed consolidated financial statements.

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**APPLERA CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**  
(Dollar amounts in thousands)

	At June 30, 2003	At September 30, 2003
	<hr/>	<hr/>
	(unaudited)	
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$ 654,283	\$ 692,480
Short-term investments	749,785	688,655
Accounts receivable, net	423,549	358,698
Inventories, net	152,060	155,433
Prepaid expenses and other current assets	93,706	102,383
	<hr/>	<hr/>
Total current assets	2,073,383	1,997,649
Property, plant and equipment, net	526,591	528,726
Other long-term assets	657,518	626,101
	<hr/>	<hr/>
<b>Total Assets</b>	<b>\$ 3,257,492</b>	<b>\$ 3,152,476</b>
	<hr/>	<hr/>
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities		
Accounts payable	\$ 166,319	\$ 137,987
Accrued salaries and wages	79,623	56,463
Accrued taxes on income	85,943	83,099
Other accrued expenses	281,435	268,263
	<hr/>	<hr/>
Total current liabilities	613,320	545,812
Long-term debt	17,101	16,880
Other long-term liabilities	286,786	272,884
	<hr/>	<hr/>
<b>Total Liabilities</b>	<b>917,207</b>	<b>835,576</b>
<b>Stockholders' Equity</b>		
Capital stock		
Applera Corporation - Applied Biosystems Group	2,128	2,130
Applera Corporation - Celera Genomics Group	723	725
Capital in excess of par value	2,102,936	2,102,000
Retained earnings	355,252	362,783
Accumulated other comprehensive loss	(54,485)	(56,469)
Treasury stock, at cost	(66,269)	(94,269)
	<hr/>	<hr/>
<b>Total Stockholders' Equity</b>	<b>2,340,285</b>	<b>2,316,900</b>
	<hr/>	<hr/>

<b>Total Liabilities and Stockholders</b>		
<b>Equity</b>	\$ 3,257,492	\$ 3,152,476

See accompanying notes to the Applera Corporation unaudited condensed consolidated financial statements.

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**APPLERA CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(unaudited)  
(Dollar amounts in thousands)

	Three months ended September 30,	
	2002	2003
	_____	_____
<b>Operating Activities of Continuing Operations</b>		
Income from continuing operations	\$ 12,065	\$ 16,012
Adjustments to reconcile income from continuing operations to net cash provided (used) by operating activities:		
Depreciation and amortization	36,091	32,286
Long-term compensation programs	2,500	1,020
Gains from investments, net		(545)
Deferred income taxes	(9,667)	(4,023)
Loss from equity method investees	4,109	762
Changes in operating assets and liabilities:		
Accounts receivable	26,632	70,458
Inventories	(9,033)	(9,482)
Prepaid expenses and other assets	(13,436)	2,705
Accounts payable and other liabilities	(52,314)	(91,721)
	_____	_____
<b>Net Cash Provided (Used) by Operating Activities of Continuing Operations</b>	(3,053)	17,472
	_____	_____
<b>Investing Activities of Continuing Operations</b>		
Additions to property, plant and equipment, net	(24,194)	(18,206)
Proceeds from short-term investments, net	107,356	76,240
Proceeds from the sale of assets, net		4,731
	_____	_____
<b>Net Cash Provided by Investing Activities of Continuing Operations</b>	83,162	62,765
	_____	_____
<b>Net Cash Used by Operating Activities of Discontinued Operations</b>	(728)	
	_____	_____
<b>Financing Activities</b>		
Net change in loans payable	9,137	
Dividends	(8,931)	(8,880)
Purchases of common stock for treasury	(6,847)	(36,295)
Proceeds from stock issued for stock plans	15,020	6,475
	_____	_____
<b>Net Cash Provided (Used) by Financing Activities</b>	8,379	(38,700)
	_____	_____
<b>Effect of Exchange Rate Changes on Cash</b>	1,206	(3,340)
	_____	_____
<b>Net Change in Cash and Cash Equivalents</b>	88,966	38,197

<b>Cash and Cash Equivalents Beginning of Period</b>	470,218	<b>654,283</b>
	<hr/>	<hr/>
<b>Cash and Cash Equivalents End of Period</b>	\$ 559,184	<b>\$ 692,480</b>
	<hr/>	<hr/>

See accompanying notes to the Applera Corporation unaudited condensed consolidated financial statements.



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**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1 ☐ Interim Condensed Consolidated Financial Statements**

We prepare our unaudited interim condensed consolidated financial statements and related disclosures in conformity with accounting principles generally accepted in the United States of America, or GAAP. In preparing these statements, we are required to use estimates and assumptions. While we believe we have considered all available information, actual results could affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. We have reclassified some prior year amounts in the condensed consolidated financial statements and notes for comparative purposes. The results for the interim periods are not necessarily indicative of trends or future financial results. When used in these notes, the terms "Applera," "Company," "we," "us," or "our" mean Applera Corporation and its subsidiaries.

We consistently applied the accounting policies described in our 2003 Annual Report to Stockholders in preparing these unaudited interim financial statements. We made all adjustments that are necessary, in our opinion, for a fair statement of the results for the interim periods. These adjustments are of a normal recurring nature. We condensed or omitted from these interim financial statements several notes and other information included in our 2003 Annual Report to Stockholders. You should read these unaudited interim condensed consolidated financial statements in conjunction with our consolidated financial statements presented in our 2003 Annual Report to Stockholders.

**Note 2 ☐ Stock-Based Compensation**

We determined pro forma income from continuing operations and earnings per share information for employee stock plans under the fair value method as required by Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation." We estimated the fair value of the options at the grant date using the Black-Scholes option-pricing model with the following weighted average assumptions for the three months ended September 30:

	2002	2003
<b>Applied Biosystems Group</b>		
Dividend yield	1.07%	<b>0.82%</b>
Volatility	72.03%	<b>71.36%</b>
Risk-free interest rate	3.01%	<b>3.18%</b>
Expected option life in years	5	<b>5</b>
<b>Celera Genomics Group</b>		
Volatility	96.88%	<b>94.56%</b>
Risk-free interest rate	3.03%	<b>3.18%</b>
Expected option life in years	4	<b>4</b>

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**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**continued**

The pro forma information for the three months ended September 30 is presented below:

(Dollar amounts in millions)	Applera Corporation	
	2002	2003
Income from continuing operations, as reported	\$ 12.1	\$ <b>16.0</b>
Add: Stock-based employee compensation expense included in reported income from continuing operations, net of tax	1.4	<b>0.6</b>
Deduct: Stock-based employee compensation expense determined under fair value based method, net of tax	38.0	<b>35.9</b>
Pro forma loss from continuing operations	\$ (24.5)	\$ <b>(19.3)</b>

(Dollar amounts in millions, except per share amounts)	Applied Biosystems Group		Celera Genomics Group	
	2002	2003	2002	2003
Income (loss) from continuing operations, as reported	\$ 34.2	\$ <b>33.4</b>	\$ (19.6)	\$ <b>(16.3)</b>
Add: Stock-based employee compensation expense included in reported income (loss) from continuing operations, net of tax	1.1	<b>0.4</b>	0.3	<b>0.2</b>
Deduct: Stock-based employee compensation expense determined under fair value based method, net of tax	29.6	<b>29.3</b>	8.4	<b>6.6</b>
Pro forma income (loss) from continuing operations	\$ 5.7	\$ <b>4.5</b>	\$ (27.7)	\$ <b>(22.7)</b>

Earnings (loss) per share from continuing operations

Basic and diluted - as reported	\$ 0.16	\$ <b>0.16</b>	\$ (0.28)	\$ <b>(0.23)</b>
Basic and diluted - pro forma	\$ 0.03	\$ <b>0.02</b>	\$ (0.39)	\$ <b>(0.31)</b>

**Note 3 □ Earnings (Loss) per Share**

The following table presents a reconciliation of basic and diluted earnings (loss) per share from continuing operations for the three months ended September 30:

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(Amounts in millions except per share amounts)	Applied Biosystems Group		Celera Genomics Group	
	2002	<b>2003</b>	2002	<b>2003</b>
Weighted average number of common shares used in the calculation of basic earnings (loss) per share	208.8	<b>208.4</b>	71.1	<b>72.2</b>
Common stock equivalents	1.2	<b>3.2</b>		
Shares used in the calculation of diluted earnings (loss) per share	210.0	<b>211.6</b>	71.1	<b>72.2</b>
Income (loss) from continuing operations used in the calculation of earnings (loss) per share from continuing operations	\$ 34.2	\$ <b>33.4</b>	\$ (19.6)	\$ <b>(16.3)</b>
Income (loss) per share from continuing operations Basic and diluted	\$ 0.16	\$ <b>0.16</b>	\$ (0.28)	\$ <b>(0.23)</b>

Options to purchase stock at exercise prices greater than the average market prices of our common stocks were excluded from the computation of diluted earnings per share because the effect would have been antidilutive. Additionally, options and warrants to purchase shares of Applera Corporation-Celera Genomics Group Common Stock (□Applera-Celera stock□) were excluded from the computation of diluted loss per share because the effect was antidilutive. The following table presents the number of shares excluded from the diluted earnings and loss per share computations.

(Shares in millions)	Three months ended September 30,	
	2002	<b>2003</b>
Applera Corporation-Applied Biosystems Group Common Stock	27.3	<b>24.7</b>
Applera-Celera stock	12.4	<b>12.2</b>

**Note 4 □ Special Charges**

During the second quarter of fiscal 2003, the Applied Biosystems group recorded pre-tax charges totaling \$33.8 million associated with the termination of approximately 400 employees, mainly in the U.S. and Europe, impairment of assets, and office closures. Positions eliminated were primarily within the areas of research, manufacturing, sales, marketing and administration. In the fourth quarter of fiscal 2003, the Applied Biosystems group recorded a pre-tax benefit of \$4.3 million for a reduction in anticipated employee-related costs associated with this program. The following table details the major components of the special charges:

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**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
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(Dollar amounts in millions)	Employee-Related Charges	Asset Impairment	Office Closures	Total
Total charges	\$ 22.9	\$ 9.5	\$ 1.4	\$ 33.8
Cash payments	15.4		0.6	16.0
Non-cash charges		9.5	0.5	10.0
Reduction of expected costs	4.3			4.3
Balance at September 30, 2003	\$ 3.2	\$	\$ 0.3	\$ 3.5

Approximately 370 employees had been terminated as of September 30, 2003. The termination of the remaining employees and the cash expenditures relating to the workforce reductions and office closures are expected to be substantially complete by the end of calendar year 2003, and will be funded primarily by cash provided by operating activities.

**Note 5 □ Comprehensive Gain (Loss)**

The components of comprehensive gain (loss) are reflected net of tax, except for foreign currency translation adjustments, which are generally not adjusted for income taxes as they relate to indefinite investments in non-U.S. subsidiaries. Comprehensive gain (loss) for the three months ended September 30 was as follows:

(Dollar amounts in millions)	Three months ended September 30,	
	2002	2003
Net income (loss)	\$ (4.3)	\$ 16.0
Other comprehensive gain (loss):		
Net unrealized gains (losses) on investments	(5.7)	1.1
Net unrealized gains on investments reclassified into earnings		(1.5)
Net unrealized gains (losses) on hedge contracts	9.3	(9.3)
Net unrealized losses on hedge contracts reclassified into earnings	1.8	2.7
Foreign currency translation adjustments	(5.4)	5.0
Total other comprehensive loss		(2.0)
Total comprehensive gain (loss)	\$ (4.3)	\$ 14.0

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**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
continued

**Note 6 □ Inventories**

Inventories included the following components:

(Dollar amounts in millions)	<b>June 30, 2003</b>	<b>September 30, 2003</b>
Raw materials and supplies	\$ 58.7	\$ <b>58.4</b>
Work-in-process	5.5	<b>3.5</b>
Finished products	87.9	<b>93.5</b>
<b>Total inventories</b>	<b>\$ 152.1</b>	<b>\$ 155.4</b>

**Note 7 □ Goodwill and Intangible Assets**

The following table presents our intangible assets subject to amortization:

(Dollar amounts in millions)	Weighted Average Life	June 30, 2003		September 30, 2003	
		Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Patents	7.5	\$ 44.7	\$ 21.2	\$ <b>44.7</b>	\$ <b>22.5</b>
Acquired technology	5.9	60.0	30.0	<b>60.0</b>	<b>31.8</b>
Favorable operating leases	4.0	11.6	4.7	<b>11.6</b>	<b>5.4</b>
<b>Total</b>		<b>\$ 116.3</b>	<b>\$ 55.9</b>	<b>\$ 116.3</b>	<b>\$ 59.7</b>

Aggregate amortization expense for the three months ended September 30 was as follows:

(Dollar amounts in millions)	2002	<b>2003</b>
Applied Biosystems group	\$ 2.4	\$ <b>2.6</b>
Celera Genomics group	2.7	<b>0.7</b>
Celera Diagnostics	0.5	<b>0.5</b>
<b>Consolidated</b>	<b>\$ 5.6</b>	<b>\$ 3.8</b>

The Applied Biosystems group records a substantial portion of amortization expense in cost of sales. The Celera Genomics group records amortization expense in amortization of intangible assets and Celera Diagnostics records amortization expense in cost of sales. Amortization expense for the Celera Genomics group in fiscal 2003 included the amortization of some intangible assets acquired as part of the Axys Pharmaceuticals, Inc. acquisition in fiscal 2002.

At September 30, 2003, we estimated annual amortization expense of our intangible assets for each of the next five fiscal years to be as shown in the following table. Future acquisitions or impairment events could cause these amounts to change.

**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
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(Dollar amounts in millions)	Applied Biosystems Group	Celera Genomics Group	Celera Diagnostics	Consolidated
2004	\$ 9.9	\$ 2.9	\$ 2.1	\$ 14.9
2005	9.3	2.9	2.1	14.3
2006	9.2	1.1	2.1	12.4
2007	8.2		2.0	10.2
2008	5.4		0.4	5.8

The carrying amount of goodwill at June 30, 2003, and September 30, 2003 was \$39.4 million, of which \$36.7 million was allocated to the Applied Biosystems group and \$2.7 million was allocated to the Celera Genomics group.

**Note 8 □ Supplemental Cash Flow Information**

Significant non-cash financing activities were as follows:

(Dollar amounts in millions)	Three months ended September 30,	
	2002	2003
Dividends declared but not paid	\$ 8.9	\$ 8.9
Issuances of restricted stock	\$ 0.2	\$ 6.6

**Note 9 □ Guarantees**

**Leases**

We provide lease-financing options to our customers through third party financing companies. For some leases, the financing companies have recourse to us for any unpaid principal balance upon default by the customer. The leases typically have terms of three years and are secured by the underlying instrument. In the event of default by a customer, we would repossess the underlying instrument. We record revenues from such transactions upon the shipment of products and maintain a reserve for estimated losses on all lease transactions with recourse provisions based on historical default rates and current economic conditions. At September 30, 2003, the financing companies' outstanding balance of lease receivables with recourse to us was \$9.8 million. We believe that we could recover the entire balance from the resale of the underlying instruments in the event of default by all customers.

**Guarantee of pension benefits for divested business**

As part of the divestiture of the Analytical Instruments business in fiscal 1999, the purchaser of the Analytical Instruments business is paying for the pension benefits for employees of a former German subsidiary. However, we guaranteed payment of these pension benefits should the purchaser fail to do so, as these benefits were not transferable to the buyer under German law. The guaranteed

**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**continued**

payment obligation, which approximated \$50 million at September 30, 2003, is not expected to have a material adverse effect on our consolidated financial position.

**Indemnifications**

In the normal course of business, we enter into some contracts under which we indemnify third parties for intellectual property infringement claims or claims arising from breaches of representations or warranties. In addition, from time to time we provide indemnity protection to third parties for claims arising from undisclosed liabilities, product liability, environmental obligations, representations and warranties, and other claims relating to past performance. In these agreements, the scope and amount of remedy, or the period in which claims can be made, may be limited. It is not possible to determine the maximum potential amount of future payments, if any, due under these indemnities due to the conditional nature of the obligations and the unique facts and circumstances involved in each agreement. Historically, payments made related to these indemnifications have not been material to our financial position.

**Product warranties**

We accrue warranty costs for product sales at the time of shipment based on historical experience as well as anticipated product performance. Our product warranties extend over a specified period of time ranging up to two years from the date of sale depending on the product subject to warranty. We periodically review the adequacy of our warranty reserve, and adjust, if necessary, the warranty percentage and accrual based on actual experience and estimated costs to be incurred.

The following table provides the analysis of the warranty reserve:

(Dollar amounts in millions)

Balance at June 30, 2003	\$ 15.1
Accruals for warranties	5.7
Usage of reserve	(7.5)
Balance at September 30, 2003	\$ 13.3

**Note 10 □ Contingencies**

**Litigation**

We are involved in various legal proceedings from time to time, including actions with respect to commercial, intellectual property, antitrust, environmental, securities, and employment matters. We believe that we have meritorious defenses against the claims currently asserted against us and intend to defend them vigorously. The following is a description of some claims we are currently defending.

Applera and some of its officers are defendants in a lawsuit purportedly brought on behalf of purchasers of Applera-Celera stock in our follow-on public offering of Applera-Celera stock completed on March 6, 2000. In the offering, we sold an aggregate of approximately 4.4 million shares of Applera-Celera stock at a public offering price of \$225 per share. The lawsuit, which was commenced with the filing of several complaints in April and May 2000, is pending in the U.S. District Court for the District of Connecticut, and an amended consolidated complaint was filed on August 21, 2001. The consolidated complaint generally alleges that the prospectus used in

**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**continued**

connection with the offering was inaccurate or misleading because it failed to adequately disclose the alleged opposition of the Human Genome Project and two of its supporters, the governments of the U.S. and the U.K., to providing patent protection to our genomic-based products. Although the Celera Genomics group has never sought, or intended to seek, a patent on the basic human genome sequence data, the complaint also alleges that we did not adequately disclose the risk that the Celera Genomics group would not be able to patent this data. The consolidated complaint seeks monetary damages, rescission, costs and expenses, and other relief as the court deems proper.

We are involved in several litigation matters with MJ Research, Inc., which commenced with our filing claims against MJ Research based on its alleged infringement of some polymerase chain reaction, or PCR, patents. In response to our claims, MJ Research filed counterclaims including, among others, allegations that we have licensed and enforced these patents through anticompetitive conduct in violation of federal and state antitrust laws, and MJ Research is seeking injunctive relief, monetary damages, costs and expenses, and other relief. Subsequently, on September 21, 2000, MJ Research filed an action against us in the U.S. District Court for the District of Columbia. This complaint is based on the allegation that the patents underlying our DNA sequencing instruments were improperly obtained because one of the alleged inventors, whose work was funded in part by the U.S. government, was knowingly omitted from the patent applications. Our patents at issue are U.S. Patent Nos. 5,171,534, entitled "Automated DNA Sequencing Technique," 5,821,058, entitled "Automated DNA Sequencing Technique," 6,200,748, entitled "Tagged Extendable Primers and Extension Products," and 4,811,218, entitled "Real Time Scanning Electrophoresis Apparatus for DNA Sequencing." The complaint asserts violations of the federal False Claims Act and the federal Bayh Dole Act, invalidity and unenforceability of the patents at issue, patent infringement, and various other civil claims against us. MJ Research is seeking monetary damages, costs and expenses, injunctive relief, transfer of ownership of the patents in dispute, and other relief as the court deems proper. MJ Research claims to be suing in the name of the U.S. government although the government has to date declined to participate in the suit. On October 9, 2003, the case against us was dismissed but the time period for appeal of that decision by MJ Research has not yet expired.

Promega Corporation filed a patent infringement action against Lifecodes Corporation, Cellmark Diagnostics, Genomics International Corporation, and us in the U.S. District Court for the Western District of Wisconsin on April 24, 2001. The complaint alleges that the defendants are infringing Promega's U.S. Patent Nos. 6,221,598 and 5,843,660, both entitled "Multiplex Amplification of Short Tandem Repeat Loci," due to the defendants' sale of forensic identification and paternity testing kits. Promega is seeking monetary damages, costs and expenses, injunctive relief, and other relief as the court deems proper. The defendants answered the complaint on July 9, 2001, and we asserted counterclaims alleging that Promega is infringing our U.S. Patent No. 6,200,748, entitled "Tagged Extendable Primers and Extension Products," due to Promega's sale of forensic identification and paternity testing kits.

Beckman Coulter, Inc. filed a patent infringement action against us in the U.S. District Court for the Central District of California on July 3, 2002. The complaint alleges that we are infringing Beckman Coulter's U.S. Patent Nos. RE 37,606 and 5,421,980, both entitled "Capillary Electrophoresis Using Replaceable Gels," and U.S. Patent No. 5,552,580, entitled "Heated Cover Device," although it does



**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
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not identify the specific facts on which this allegation is based. Since Beckman Coulter filed this claim, U.S. Patent No. 5,421,980 has been reissued as U.S. Patent No. RE 37,941, entitled "Capillary Electrophoresis Using Replaceable Gels." On January 13, 2003, the court permitted Beckman Coulter to make a corresponding amendment to its complaint. Beckman Coulter is seeking monetary damages, costs and expenses, injunctive relief, and other relief as the court deems proper. On February 10, 2003, we filed our answer to Beckman Coulter's allegations, and counterclaimed for declaratory relief that the Beckman Coulter patents underlying Beckman Coulter's claim are invalid, unenforceable, and not infringed. We are seeking dismissal of Beckman Coulter's complaint, costs and expenses, declaratory and injunctive relief, and other relief as the court deems proper.

Henry Huang (an individual) filed an action against us and the Applied Biosystems group and the other parties described below in the U.S. District Court for the Central District of California on February 19, 2003. Mr. Huang's complaint seeks to change inventorship of the patents described below, and claims breach of contract, fraud, conversion, and unjust enrichment. The complaint relates to U.S. Patent Nos. 5,171,534, entitled "Automated DNA Sequencing Technique," 5,821,058, entitled "Automated DNA Sequencing Technique," 6,200,748, entitled "Tagged Extendable Primers and Extension Products," and 4,811,218, entitled "Real Time Scanning Electrophoresis Apparatus for DNA Sequencing." U.S. Patent Nos. 5,171,534, 5,821,058, and 6,200,748 are assigned to the California Institute of Technology and licensed by the Applied Biosystems group. U.S. Patent No. 4,811,218 is assigned to the Applied Biosystems group. Also named in the complaint are the California Institute of Technology, Lloyd Smith, Leroy Hood, Michael Hunkapiller, Timothy Hunkapiller, Charles Connell, John Lytle, William Mordan, and John Bridgham. Lloyd Smith, Leroy Hood, Michael Hunkapiller, Timothy Hunkapiller, and Charles Connell are the inventors named on U.S. Patent Nos. 5,171,534, 5,821,058, and 6,200,748. Michael Hunkapiller, Charles Connell, John Lytle, William Mordan, and John Bridgham are the inventors named on U.S. Patent No. 4,811,218. The issues involved in this litigation are related to the issues in the MJ Research, Inc. litigation that was filed September 21, 2000, which is described above. Mr. Huang is alleging that he is the sole inventor on U.S. Patent Nos. 5,171,534, 5,821,058, 6,200,748, and 4,811,218. He is seeking to substitute himself for the named inventors on the relevant patents, and to have himself named as the sole assignee of the patents, and is also seeking monetary damages, costs, expenses, and other relief as the court deems proper.

Genetic Technologies Limited filed a patent infringement action against us in the U.S. District Court for the Northern District of California on March 26, 2003. They filed an amended complaint against us on August 12, 2003. The amended complaint alleges that we are infringing U.S. Patent No. 5,612,179, entitled "Intron Sequence Analysis Method for Detection of Adjacent and Remote Locus Alleles as Haplotypes," and U.S. Patent No. 5,851,762, entitled "Genomic Mapping Method by Direct Haplotyping Using Intron Sequence Analysis." The allegedly infringing products are cystic fibrosis reagent kits, Assays-on-Demand products for non-coding regions, Assays-by-Design<sup>SM</sup> services for non-coding regions, and the Celera Discovery System. The complaint also alleges that haplotyping analysis performed by our businesses infringes the patents identified above. Genetic Technologies Limited is seeking monetary damages, costs, expenses, injunctive relief, and other relief as the court deems proper.

**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
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On-Line Technologies, Inc. (since acquired by MKS Instruments, Inc.) filed claims for patent infringement, trade secret misappropriation, fraud, breach of contract and unfair trade practices against PerkinElmer, Inc., Sick UPA, GmbH, and us in the U.S. District Court for the District of Connecticut on or about November 3, 1999. The complaint alleged that products called the Spectrum One and the MCS100E manufactured by former divisions of the Applied Biosystems group, which divisions were sold to the co-defendants in this case, were based on allegedly proprietary information belonging to On-Line Technologies and that the MCS100E infringed U.S. Patent No. 5,440,143. On-Line Technologies sought monetary damages, costs, expenses, injunctive relief, and other relief. On April 2, 2003, the U.S. District Court for the District of Connecticut granted our summary judgment motion and dismissed all claims brought by On-Line Technologies, Inc., though On-Line Technologies has filed an appeal with the U.S. Court of Appeals for the Federal Circuit seeking reinstatement of its claims.

We have not accrued for any potential losses in the cases described above because we believe that an adverse determination is not probable, and potential losses cannot be reasonably estimated, in any of these cases. However, the outcome of litigation is inherently uncertain, and we cannot be sure that we will prevail in any of the cases described above or in our other current litigation. An adverse determination in some of our current litigation, particularly the cases described above, could have a material adverse effect on our consolidated financial statements.

In addition, we note that we filed claims against Roche Molecular Systems, Inc., Hoffman-La Roche, Inc., Roche Probe, Inc., F. Hoffman La-Roche Ltd., and other potential defendants affiliated with the named defendants in California Superior Court on October 9, 2003. Our complaint asserts, among other things, breach of contract and other contract claims against the defendants arising from agreements relating to polymerase chain reaction, or PCR, technology rights entered into between us and the defendants. Our complaint also asserts various tort claims against the defendants, including breach of trust, breach of fiduciary duty, and unfair competition, relating to our PCR rights. The defendants' acts and omissions that form the basis of the complaint include, among other things, the: (i) defendants' failure to abide by contractual provisions intended to allow us to effectively compete with the defendants with respect to (a) sales of diagnostic PCR products and (b) conveyance of diagnostic PCR rights to third parties; (ii) defendants' failure to pay us requisite royalties for sales by them of thermal cyclers and other products; (iii) defendants' failure to negotiate in good faith new agreements directed at modifying the relationship between the parties in accordance with principles set forth in an existing agreement that states the intended framework for the negotiations; (iv) defendants' failure to provide us with diagnostic PCR rights on a nondiscriminatory basis as required by a European Union commission decree; (v) defendants' failure to comply with their agreement to assign ownership to us of some PCR instrument patents and patent applications, and (vi) defendants' mishandling of the prosecution of patent applications that the defendants were obligated to assign to us, in a manner that damaged us and precluded us from obtaining the full potential scope of patent protection for our instrument rights. Contemporaneously with our filing of this complaint, we also commenced arbitration proceedings with the American Arbitration Association against the defendants asserting, among other things, patent infringement claims (both direct infringement, contributory infringement and infringement by inducing third parties to infringe), breach of contract and other contract claims, and tort claims such as breach of fiduciary duty, breach of trust, and unfair

**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**continued**

competition. The arbitration is based on our allegation that the defendants (i) have infringed our exclusive rights to PCR patents in fields exclusively licensed to us pursuant to agreements with the defendants; and (ii) by their acts and omissions, have undermined the value of our exclusive PCR rights. In both the legal complaint and the arbitration, we are seeking monetary damages, costs, expenses, injunctive relief, and other relief as the court or arbitrator deems proper.

**Discontinued Operations**

We recorded a charge of \$16.4 million, net of income taxes, as part of discontinued operations in the first quarter of fiscal 2003. This charge relates to an adverse jury verdict we received in October 2002, in connection with a patent lawsuit between TA Instruments, Inc., a subsidiary of Waters Corporation, and The Perkin-Elmer Corporation relating to thermal analysis products. The Applied Biosystems group is involved as the successor to The Perkin-Elmer Corporation, having sold the thermal instruments product line as part of the sale of its Analytical Instruments business to EG&G, Inc. (now named PerkinElmer, Inc.) in 1999. This award is subject to entry of a final order by the court, where interest and additional damages may be added. We have appealed the judgment with the U.S. Court of Appeals for the Federal Circuit.

**Note 11 □ Segment and Consolidating Information**

Presented below is our segment and consolidating financial information, including the allocation of expenses between the segments in accordance with our allocation policies, as well as other related party transactions, such as sales of products between segments. Our board of directors approves the method of allocating earnings to each class of common stock for purposes of calculating earnings per share. This determination is generally based on net income or loss amounts of the corresponding group calculated in accordance with GAAP, consistently applied.

See Note 15 to our consolidated financial statements included in our 2003 Annual Report to Stockholders for a detailed description of the segments and the management and allocation policies applicable to the attribution of assets, liabilities, revenues and expenses to the segments (which information is incorporated herein by reference).

**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**continued**

(Dollar amounts in millions)	Three Months Ended September 30,	
	2002	<b>2003</b>
<hr/>		
<b>Applied Biosystems Group</b>		
Sales to the Celera Genomics group (1)	\$ 0.9	\$ <b>0.3</b>
Sales to Celera Diagnostics (1)	0.9	<b>2.6</b>
Nonreimbursable utilization of tax benefits (2)	9.7	<b>6.1</b>
Payments for reimbursable utilization of tax benefits (3)	6.0	<b>5.3</b>
Funding of Celera Diagnostics (4)	1.8	<b>2.2</b>
<hr/>		
<b>Celera Genomics Group</b>		
Revenues from royalties (5)	\$ 0.4	\$ <b>0.6</b>
Funding of Celera Diagnostics (6)	14.2	<b>12.5</b>
<hr/>		
<b>Celera Diagnostics</b>		
Sales to the Applied Biosystems group (7)	\$ 3.0	\$ □
<hr/>		

- (1) The Applied Biosystems group recorded net revenues from leased instruments, consumables, and project materials to the Celera Genomics group and Celera Diagnostics.
- (2) The Applied Biosystems group used, without reimbursement, some of the tax benefits generated by the Celera Genomics group in accordance with our tax allocation policy.
- (3) The Applied Biosystems group paid the Celera Genomics group for the use of existing tax benefits acquired by the Celera Genomics group in business combinations and other tax benefits, including those associated with Celera Diagnostics in accordance with our tax allocation policy.
- (4) The Applied Biosystems group recorded its share of capital expenditures and working capital funding for Celera Diagnostics.
- (5) The Celera Genomics group recorded net revenues primarily for royalties generated by sales of some of the products of the Knowledge Business under an online marketing and distribution agreement with the Applied Biosystems group.
- (6) The Celera Genomics group recorded operating losses and its share of capital expenditures and working capital funding for Celera Diagnostics.
- (7) Celera Diagnostics recorded net revenues from the sale of diagnostics products to the Applied Biosystems group under a distribution agreement. On October 1, 2002, sales responsibilities for products manufactured by Celera Diagnostics were largely transferred to the diagnostic division of Abbott Laboratories, pursuant to the profit-sharing alliance announced on June 30, 2002.

**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**continued**

For the three month periods ended September 30, 2002 and 2003, the Celera Genomics group recorded 100% of the losses of Celera Diagnostics in its net loss as well as the tax benefit associated with those losses. In the following tables, the "Eliminations" column represents the elimination of intersegment activity and the losses of Celera Diagnostics, which are included both in the "Celera Diagnostics" column and net within the "Celera Genomics group" column as "Loss from joint venture."

**Condensed Consolidating Statement of Operations for the Three Months Ended September 30, 2003**

(Dollar amounts in thousands)	Applied Biosystems Group	Celera Genomics Group	Celera Diagnostics	Eliminations	Consolidated
Net revenues from external customers	\$ 379,723	\$ 16,806	\$ 8,508	\$ □	\$ 405,037
Intersegment revenues	2,948	551	13	(3,512)	
<b>Net Revenues</b>	<b>382,671</b>	<b>17,357</b>	<b>8,521</b>	<b>(3,512)</b>	<b>405,037</b>
Cost of sales	186,290	2,722	3,655	(2,189)	190,478
<b>Gross Margin</b>	<b>196,381</b>	<b>14,635</b>	<b>4,866</b>	<b>(1,323)</b>	<b>214,559</b>
Selling, general and administrative	85,273	6,749	3,844	11,491	107,357
Corporate allocated expenses	9,358	1,477	656	(11,491)	
Research, development and engineering	59,597	21,750	12,422	(1,357)	92,412
Amortization of intangible assets		725			725
<b>Operating Income (Loss)</b>	<b>42,153</b>	<b>(16,066)</b>	<b>(12,056)</b>	<b>34</b>	<b>14,065</b>
Gain (loss) on investments, net	1,188	(643)			545
Interest income, net	2,933	3,137			6,070
Other income (expense), net	84	(1,070)			(986)
Loss from joint venture		(12,056)		12,056	
<b>Income (Loss) before Income Taxes</b>	<b>46,358</b>	<b>(26,698)</b>	<b>(12,056)</b>	<b>12,090</b>	<b>19,694</b>
Provision (benefit) for income taxes	12,980	(10,412)		1,114	3,682
<b>Net Income (Loss)</b>	<b>\$ 33,378</b>	<b>\$ (16,286)</b>	<b>\$ (12,056)</b>	<b>\$ 10,976</b>	<b>\$ 16,012</b>

**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
*continued*

**Condensed Consolidating Statement of Financial Position at September 30, 2003**

(Dollar amounts in thousands)	Applied Biosystems Group	Celera Genomics Group	Celera Diagnostics	Eliminations	Consolidated
<b>Assets</b>					
Current assets					
Cash and cash equivalents	\$ 590,794	\$ 101,686	\$ □	\$ □	\$ 692,480
Short-term investments		688,655			688,655
Accounts receivable, net	345,668	8,160	5,583	(713)	358,698
Inventories, net	142,197	2,339	11,036	(139)	155,433
Prepaid expenses and other current assets	91,939	14,253	855	(4,664)	102,383
<b>Total current assets</b>	<b>1,170,598</b>	<b>815,093</b>	<b>17,474</b>	<b>(5,516)</b>	<b>1,997,649</b>
Property, plant and equipment, net	417,000	100,619	11,424	(317)	528,726
Other long-term assets	475,824	167,473	8,182	(25,378)	626,101
<b>Total Assets</b>	<b>\$ 2,063,422</b>	<b>\$ 1,083,185</b>	<b>\$ 37,080</b>	<b>\$ (31,211)</b>	<b>\$ 3,152,476</b>
<b>Liabilities and Stockholders' Equity</b>					
Current liabilities					
Accounts payable	\$ 130,875	\$ 4,471	\$ 7,765	\$ (5,124)	\$ 137,987
Accrued salaries and wages	45,841	8,430	2,192		56,463
Accrued taxes on income	70,575	12,524			83,099
Other accrued expenses	225,021	41,763	1,732	(253)	268,263
<b>Total current liabilities</b>	<b>472,312</b>	<b>67,188</b>	<b>11,689</b>	<b>(5,377)</b>	<b>545,812</b>
Long-term debt		16,880			16,880
Other long-term liabilities	253,486	18,647	751		272,884
<b>Total Liabilities</b>	<b>725,798</b>	<b>102,715</b>	<b>12,440</b>	<b>(5,377)</b>	<b>835,576</b>
<b>Total Stockholders' Equity</b>	<b>1,337,624</b>	<b>980,470</b>	<b>24,640</b>	<b>(25,834)</b>	<b>2,316,900</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$ 2,063,422</b>	<b>\$ 1,083,185</b>	<b>\$ 37,080</b>	<b>\$ (31,211)</b>	<b>\$ 3,152,476</b>

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**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
continued

**Condensed Consolidating Statement of Cash Flows for the Three Months Ended September 30, 2003**

(Dollar amounts in thousands)	Applied Biosystems Group	Celera Genomics Group	Celera Diagnostics	Eliminations	Consolidated
<b>Operating Activities</b>					
Net income (loss)	\$ 33,378	\$ (16,286)	\$ (12,056)	\$ 10,976	\$ 16,012
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:					
Depreciation and amortization	24,990	5,507	1,823	(34)	32,286
Long-term compensation programs	736	284			1,020
(Gains) losses on investments	(1,188)	643			(545)
Deferred income taxes	(5,168)	59		1,086	(4,023)
Loss from joint venture and equity method investees		12,818		(12,056)	762
Nonreimbursable utilization of intergroup tax benefits	6,079	(6,079)			
Changes in operating assets and liabilities:					
Accounts receivable	64,867	8,548	(480)	(2,477)	70,458
Inventories	(7,473)	187	(2,196)		(9,482)
Prepaid expenses and other assets	3,392	(3,299)	(169)	2,781	2,705
Accounts payable and other liabilities	(71,977)	(18,010)	(1,458)	(276)	(91,721)
<b>Net Cash Provided (Used) by Operating Activities</b>	47,636	(15,628)	(14,536)	□	17,472
<b>Investing Activities</b>					
Additions to property, plant and equipment, net	(17,196)	(857)	(156)	3	(18,206)
Proceeds from short-term investments, net		76,240			76,240
Investments in joint venture	(2,229)	(12,463)		14,692	
Proceeds from the sale of assets, net	4,123	611		(3)	4,731
<b>Net Cash Provided (Used) by Investing Activities</b>	(15,302)	63,531	(156)	14,692	62,765
<b>Financing Activities</b>					
Dividends	(8,880)				(8,880)
Net cash funding from groups			14,692	(14,692)	
Purchases of common stock for treasury	(36,295)				(36,295)

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Proceeds from stock issued for stock plans	5,309	1,166			6,475
<b>Net Cash Provided (Used) by Financing Activities</b>	(39,866)	1,166	14,692	(14,692)	(38,700)
<b>Effect of Exchange Rate Changes on Cash</b>	(3,340)				(3,340)
<b>Net Change in Cash and Cash Equivalents</b>	(10,872)	49,069	□	□	38,197
<b>Cash and Cash Equivalents Beginning of Period</b>	601,666	52,617			654,283
<b>Cash and Cash Equivalents End of Period</b>	\$ 590,794	\$ 101,686	\$ □	\$ □	692,480



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**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
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**Condensed Consolidating Statement of Operations for the Three Months Ended September 30, 2002**

(Dollar amounts in thousands)	Applied Biosystems Group	Celera Genomics Group	Celera Diagnostics	Eliminations	Consolidated
Net revenues from external customers	\$ 394,118	\$ 23,186	\$ 29	\$ □	\$ 417,333
Intersegment revenues	1,779	462	2,951	(5,192)	
<b>Net Revenues</b>	395,897	23,648	2,980	(5,192)	417,333
Cost of sales	193,298	3,418	2,417	(4,239)	194,894
<b>Gross Margin</b>	202,599	20,230	563	(953)	222,439
Selling, general and administrative	87,486	5,036	2,169	13,410	108,101
Corporate allocated expenses	10,790	1,956	664	(13,410)	
Research, development and engineering	61,032	32,533	11,063	(1,337)	103,291
Amortization of intangible assets		2,700			2,700
<b>Operating Income (Loss)</b>	43,291	(21,995)	(13,333)	384	8,347
Interest income, net	3,194	5,185			8,379
Other income (expense), net	1,045	(3,160)			(2,115)
Loss from joint venture		(13,333)		13,333	
<b>Income (Loss) before Income Taxes</b>	47,530	(33,303)	(13,333)	13,717	14,611
Provision (benefit) for income taxes	13,308	(13,654)		2,892	2,546
<b>Income (Loss) from Continuing Operations</b>	34,222	(19,649)	(13,333)	10,825	12,065
Loss from discontinued operations, net of income taxes	(16,400)				(16,400)
<b>Net Income (Loss)</b>	\$ 17,822	\$ (19,649)	\$ (13,333)	\$ 10,825	\$ (4,335)

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**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
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**Consolidating Statement of Financial  
Position at June 30, 2003**

(Dollar amounts in thousands)	Applied Biosystems Group	Celera Genomics Group	Celera Diagnostics	Eliminations	Consolidated
<b>Assets</b>					
Current assets					
Cash and cash equivalents	\$ 601,666	\$ 52,617	\$ □	\$ □	\$ 654,283
Short-term investments		749,785			749,785
Accounts receivable, net	404,928	16,708	5,103	(3,190)	423,549
Inventories, net	140,833	2,526	8,840	(139)	152,060
Prepaid expenses and other current assets	84,393	10,510	686	(1,883)	93,706
<b>Total current assets</b>	<b>1,231,820</b>	<b>832,146</b>	<b>14,629</b>	<b>(5,212)</b>	<b>2,073,383</b>
Property, plant and equipment, net	409,626	104,742	12,574	(351)	526,591
Other long-term assets	485,269	185,178	8,699	(21,628)	657,518
<b>Total Assets</b>	<b>\$ 2,126,715</b>	<b>\$ 1,122,066</b>	<b>\$ 35,902</b>	<b>\$ (27,191)</b>	<b>\$ 3,257,492</b>
<b>Liabilities and Stockholders' Equity</b>					
Current liabilities					
Accounts payable	\$ 153,124	\$ 10,241	\$ 7,651	\$ (4,697)	\$ 166,319
Accrued salaries and wages	63,859	11,886	3,878		79,623
Accrued taxes on income	73,611	12,332			85,943
Other accrued expenses	232,674	46,907	2,230	(376)	281,435
<b>Total current liabilities</b>	<b>523,268</b>	<b>81,366</b>	<b>13,759</b>	<b>(5,073)</b>	<b>613,320</b>
Long-term debt		17,101			17,101
Other long-term liabilities	265,274	21,373	139		286,786
<b>Total Liabilities</b>	<b>788,542</b>	<b>119,840</b>	<b>13,898</b>	<b>(5,073)</b>	<b>917,207</b>
<b>Total Stockholders' Equity</b>	<b>1,338,173</b>	<b>1,002,226</b>	<b>22,004</b>	<b>(22,118)</b>	<b>2,340,285</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$ 2,126,715</b>	<b>\$ 1,122,066</b>	<b>\$ 35,902</b>	<b>\$ (27,191)</b>	<b>\$ 3,257,492</b>

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**APPLERA CORPORATION**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
continued

**Condensed Consolidating Statement of Cash Flows for the Three Months Ended September 30, 2002**

(Dollar amounts in thousands)	Applied Biosystems Group	Celera Genomics Group	Celera Diagnostics	Eliminations	Consolidated
<b>Operating Activities of Continuing Operations</b>					
Income (loss) from continuing operations	\$ 34,222	\$ (19,649)	\$ (13,333)	\$ 10,825	\$ 12,065
Adjustments to reconcile income (loss) from continuing operations to net cash provided (used) by operating activities:					
Depreciation and amortization	23,588	12,074	911	(482)	36,091
Long-term compensation programs	1,930	570			2,500
Deferred income taxes	(13,131)	761		2,703	(9,667)
Loss from joint venture and equity method investees		17,442		(13,333)	4,109
Nonreimbursable utilization of intergroup tax benefits	9,716	(9,716)			
Changes in operating assets and liabilities:					
Accounts receivable	8,252	17,362	(17)	1,035	26,632
Inventories	(8,117)	(270)	(643)	(3)	(9,033)
Prepaid expenses and other assets	(11,608)	(1,351)	(471)	(6)	(13,436)
Accounts payable and other liabilities	(29,247)	(21,303)	(1,025)	(739)	(52,314)
<b>Net Cash Provided (Used) by Operating Activities of Continuing Operations</b>	15,605	(4,080)	(14,578)	□	(3,053)
<b>Investing Activities of Continuing Operations</b>					
Additions to property, plant and equipment, net	(20,908)	(1,871)	(1,415)		(24,194)
Proceeds from short-term investments, net		107,356			107,356
Investments in joint venture	(1,786)	(14,207)		15,993	
<b>Net Cash Provided (Used) by Investing Activities of Continuing Operations</b>	(22,694)	91,278	(1,415)	15,993	83,162
<b>Net Cash Used by Operating Activities of Discontinued Operations</b>	(728)				(728)

**Financing Activities**

Net change in loans payable	9,137				9,137
Dividends	(8,931)				(8,931)
Net cash funding from groups			15,993	(15,993)	
Purchases of common stock for treasury	(6,847)				(6,847)
Proceeds from stock issued for stock plans	3,387	11,633			15,020

**Net Cash Provided (Used)  
by Financing Activities**

(3,254)	11,633	15,993	(15,993)	8,379
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**Effect of Exchange Rate  
Changes on Cash**

1,206				1,206
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**Net Change in Cash and  
Cash Equivalents**  
**Cash and Cash Equivalents  
Beginning of Period**

(9,865)	98,831	□	□	88,966
441,328	28,890			470,218

**Cash and Cash Equivalents  
End of Period**

\$ 431,463	\$ 127,721	\$ □	\$ □	\$ 559,184
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**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

**APPLERA CORPORATION  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND  
RESULTS OF OPERATIONS**

The purpose of the following management's discussion and analysis is to provide an overview of the business of Applera Corporation to help facilitate an understanding of significant factors influencing our historical operating results, financial condition and cash flows and also to convey our expectations of the potential impact of known trends, events or uncertainties that may impact our future results. You should read this discussion in conjunction with our consolidated financial statements and related notes included in this report and in our 2003 Annual Report to Stockholders. Historical results and percentage relationships are not necessarily indicative of operating results for future periods. When used in the management discussion, the terms "Applera," "Company," "we," "us," or "our" mean Applera Corporation and its subsidiaries.

**Overview**

We are comprised of three business segments: the Applied Biosystems group, the Celera Genomics group, and Celera Diagnostics.

The Applied Biosystems group serves the life science industry and research community by developing and marketing instrument-based systems, consumables, software, and services. Customers use these tools to analyze nucleic acids (DNA and RNA), small molecules, and proteins to make scientific discoveries, develop new pharmaceuticals, and conduct standardized testing.

The Celera Genomics group is engaged principally in integrating advanced technologies to discover and develop new therapeutics. The Celera Genomics group intends to leverage its proteomic, bioinformatic, and genomic capabilities to identify and validate drug targets, and to discover and develop new therapeutics. Its Celera Discovery System™ online platform, marketed exclusively through the Applied Biosystems group's Knowledge Business, is an integrated source of information based on the human genome and other biological and medical sources.

Celera Diagnostics, a 50/50 joint venture between the Applied Biosystems group and the Celera Genomics group, is focused on the discovery, development, and commercialization of novel diagnostic products.

In fiscal 1999, as part of a recapitalization of our Company, we created two classes of common stock referred to as "tracking" stocks. Tracking stock is a class of stock of a corporation intended to "track" or reflect the performance of a specific business within the corporation.

Applera Corporation-Applied Biosystems Group Common Stock ("Applera-Applied Biosystems stock") is listed on the New York Stock Exchange under the ticker symbol "ABI" and is intended to reflect the relative performance of the Applied Biosystems group. Applera Corporation-Celera Genomics Group Common Stock ("Applera-Celera stock") is listed on the New York Stock Exchange under the ticker symbol "CRA" and is intended to reflect the relative performance of the

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**APPLERA CORPORATION**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND**  
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Celera Genomics group. There is no single security that represents the performance of Applera Corporation as a whole, nor is there a separate security traded for Celera Diagnostics.

Holders of Applera-Applied Biosystems stock and Applera-Celera stock are stockholders of Applera. The Applied Biosystems group and the Celera Genomics group are not separate legal entities, and holders of these stocks are stockholders of a single company, Applera. As a result, holders of these stocks are subject to all of the risks associated with an investment in Applera and all of its businesses, assets, and liabilities. The Applied Biosystems group and the Celera Genomics group do not have separate boards of directors. Applera has one board of directors, which will make any decision in accordance with its good faith business judgment that the decision is in the best interests of Applera and all of its stockholders as a whole.

More information about the risks relating to our capital structure, particularly our two classes of capital stock, is contained in our most recent Annual Report on Form 10-K filed with the Securities and Exchange Commission.

Our fiscal year ends on June 30. The financial information for each segment is presented in Note 11 to our condensed consolidated financial statements, Segment and Consolidating Information. Management's discussion and analysis addresses the consolidated financial results followed by the discussions of our three segments.

The following noteworthy developments have occurred since the beginning of fiscal 2004:

*Applied Biosystems Group*

- In September 2003, Catherine M. Burzik joined the Applied Biosystems group as Executive Vice President, responsible for global commercial activities, and became a member of the Applera Executive Committee.
- Also in September 2003, the Applied Biosystems group announced the introduction of the 8500 Affinity Chip Analyzer, which rapidly identifies and characterizes antibody diagnostic and therapeutic candidates.

*Celera Diagnostics*

- In September 2003, Celera Diagnostics announced the discovery of several novel genetic markers associated with an increased risk for myocardial infarction, or heart attack.
- In October 2003, Celera Diagnostics announced a research collaboration with Merck & Co. to identify and validate genetic markers useful in the development of prognostic tests and therapeutics for selected cancers.

**Critical Accounting Policies**

Please refer to the discussion of our critical accounting policies contained in the management's discussion and analysis section of our 2003 Annual Report to Stockholders (which discussion is incorporated herein by reference).

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**APPLERA CORPORATION**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND**  
**RESULTS OF OPERATIONS continued**

**Events Impacting Comparability**

We are providing the following information on some items that represent actions taken by us or events that occurred in the periods indicated. We describe the effect of these items on our reported earnings for the purpose of providing you with a better understanding of our on-going operations. You should consider these items when making comparisons to past performance and assessing prospects for future results.

***Acquired In-Process Research and Development***

During fiscal 2002, we acquired Axys Pharmaceuticals, Inc. and recorded a charge to write off the value of acquired in-process research and development (IPR&D). As of the acquisition date, the technological feasibility of the related projects had not been established, and it was determined that the acquired projects had no future alternative uses.

The Axys projects acquired as part of the acquisition are in various stages of research and development or are no longer being pursued. The continuing projects will require additional research and development efforts by the Celera Genomics group or its collaborators before any eventual products can be marketed, if ever. These efforts include extensive pre-clinical and clinical testing and are subject to lengthy regulatory review and clearance or approval by the U.S. Food and Drug Administration. The nature and timing of these remaining efforts are dependent on successful testing and clearance or approval of the products as well as maintaining the existing collaborative relationships and entering into new collaborative relationships. If collaboration partners terminate or elect to cancel their agreements or otherwise fail to conduct their collaborative activities in a timely manner, the development or commercialization process could be delayed or abandoned.

During the first quarter of fiscal 2004, we continued to pursue all acquired projects that were active as of June 30, 2003, and the pre-clinical studies for these projects are expected to continue through fiscal 2004, with the anticipation that at least one of the compounds, most likely from one of the partnered projects, could enter clinical trials during fiscal 2004. The Celera Genomics group's partners will make clinical development decisions with respect to partnered compounds.

The costs to complete the proprietary projects depend on how the Celera Genomics group decides to commercialize the projects, including whether to partner the project, and at what stage to partner. The Celera Genomics group has in the past reviewed and continues to review the proprietary pre-clinical projects. These reviews may lead to revised prioritization, resourcing and strategies to move toward clinical trials and commercialization. As a result of these actions, actual results for some programs have varied, and for others in the future may vary, from the valuation assumptions outlined in Note 2 to our consolidated financial statements contained in our 2003 Annual Report to Stockholders.

**APPLERA CORPORATION**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND**  
**RESULTS OF OPERATIONS** *continued*

**Other Special Charges**

During the second quarter of fiscal 2003, the Applied Biosystems group recorded pre-tax charges totaling \$33.8 million associated with the termination of approximately 400 employees, mainly in the U.S. and Europe, impairment of assets, and office closures. Positions eliminated were primarily within the areas of research, manufacturing, sales, marketing and administration. In the fourth quarter of fiscal 2003, the Applied Biosystems group recorded a pre-tax benefit of \$4.3 million for a reduction in anticipated employee-related costs associated with this program. The following table details the major components of the special charges:

(Dollar amounts in millions)	Employee- Related Charges	Asset Impairment	Office Closures	Total
Total charges	\$ 22.9	\$ 9.5	\$ 1.4	\$ 33.8
Cash payments	15.4		0.6	16.0
Non-cash charges		9.5	0.5	10.0
Reduction of expected costs	4.3			4.3
Balance at September 30, 2003	\$ 3.2	\$ 0	\$ 0.3	\$ 3.5

Approximately 370 employees had been terminated as of September 30, 2003. The termination of the remaining employees and the cash expenditures relating to the workforce reductions and office closures are expected to be substantially complete by the end of calendar year 2003, and will be funded primarily by cash provided by operating activities.

**Discussion of Consolidated Operations****Results of Continuing Operations—The Three Months Ended September 30, 2003 Compared with the Three Months Ended September 30, 2002**

(Dollar amounts in millions)	2002	2003	% Increase/ (Decrease)
Net revenues	\$ 417.3	\$ 405.0	(2.9%)
Cost of sales	194.9	190.4	(2.3%)
Gross margin	222.4	214.6	(3.5%)
SG&A expenses	108.1	107.4	(0.6%)
R&D	103.3	92.4	(10.6%)
Amortization of intangible assets	2.7	0.7	(74.1%)
Operating income	8.3	14.1	69.9%
Gain on investments, net		0.5	
Interest income, net	8.4	6.0	(28.6%)
Other income (expense), net	(2.1)	(0.9)	(57.1%)
Income before income taxes	14.6	19.7	34.9%
Provision for income taxes	2.5	3.7	48.0%
Income from continuing operations	\$ 12.1	\$ 16.0	32.2%





**APPLERA CORPORATION**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND**  
**RESULTS OF OPERATIONS continued**

We reported income from continuing operations of \$16.0 million in the first quarter of fiscal 2004 compared with \$12.1 million in the first quarter of fiscal 2003. The increase in income from continuing operations reflected lower R&D expenses, partially offset by lower net revenues and net interest income. The effect of foreign currency increased income from continuing operations in the first quarter of fiscal 2004 by approximately 12% compared to the prior year quarter. Please refer to the discussion on pages 29 to 36 of this quarterly report for further information on the financial results of our segments.

Net revenues in the first quarter of fiscal 2004 decreased compared with the prior year quarter. Revenues decreased at the Applied Biosystems group, due primarily to lower sequencing-related revenues caused by delays in government funding, which resulted in reduced purchases by large genome centers. In addition, manufacturing capabilities of the Applied Biosystems/MDS Sciex joint venture could not fulfill stronger than expected demand for the recently introduced 4000 Q TRAP<sup>®</sup> LC/MS/MS System. Fiscal 2003 first quarter revenue for the Applied Biosystems group included \$5.4 million for a license relating to some mass spectrometry technology and \$3.9 million of end-user sales of Celera Diagnostics products that are now distributed by Abbott Laboratories rather than the Applied Biosystems group. Net revenues also decreased at the Celera Genomics group, primarily resulting from the contractual expiration of various Online/Information Business customer agreements. The favorable effects of foreign currency increased net revenues by approximately 2% compared to the prior year quarter.

Gross margin, as a percentage of net revenues, was 53.0% for the first quarter of fiscal 2004 compared with 53.3% for the first quarter of fiscal 2003. The lower gross margin percentage in fiscal 2004 was due primarily to a change in product sales mix at the Applied Biosystems group and lower revenues at the Celera Genomics group, partially offset by the favorable effects of foreign currency.

SG&A expenses, as a percentage of net revenues, increased to 26.5% for the first quarter of fiscal 2004 compared to 25.9% for the first quarter of fiscal 2003 primarily due to increased pension, insurance and legal expenses at the Applied Biosystems group, higher employee-related costs, including severance, at the Celera Genomics group, and a \$1.1 million charge related to a facility lease agreement at Celera Diagnostics, partially offset by the reduction in personnel announced in December 2002 at the Applied Biosystems group.

R&D expenses decreased by \$10.9 million for the first quarter of fiscal 2004 to \$92.4 million from \$103.3 million for the first quarter of fiscal 2003. This decrease was primarily due to the completion of the Applera Genomics Initiative, the costs of which were shared among our three businesses, and programs eliminated at the Celera Genomics group resulting from the June 2002 restructuring and related transformation of the business, lower Online/Information Business R&D, and \$2.9 million recorded in the first quarter of fiscal 2003 for asset write-downs associated with the Rockville sequencing facility. This decrease was partially offset by continued spending on the development of new products and technologies by the Applied Biosystems group and diagnostics discovery and development programs by Celera Diagnostics.

**APPLERA CORPORATION**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND**  
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Interest income, net decreased slightly primarily due to lower average interest rates and, to a lesser extent, lower average cash and cash equivalents and short-term investments balances during the first quarter of fiscal 2004 compared to the prior year quarter.

The increase in the effective tax rate is primarily due to changes in forecasted R&D credits.

**Applera Corporation**

**Discussion of Condensed Consolidated Financial Resources and Liquidity**

We had cash and cash equivalents and short-term investments of \$1.4 billion at September 30, 2003 and June 30, 2003. We maintain a \$50 million revolving credit agreement with three banks that expires on April 20, 2005, under which there were no borrowings outstanding at September 30, 2003. Cash provided by operating activities has been our primary source of funds over the last fiscal year.

We believe that existing funds, cash generated from operations, and existing sources of debt financing are adequate to satisfy our normal operating cash flow needs, planned capital expenditures, dividends, and planned share repurchases for the foreseeable future. However, we may raise additional capital from time to time.

(Dollar amounts in millions)	June 30, 2003	September 30, 2003
Cash and cash equivalents	\$ 654.3	\$ <b>692.5</b>
Short-term investments	749.8	<b>688.6</b>
<b>Total cash and cash equivalents and short-term investments</b>	<b>\$ 1,404.1</b>	<b>\$ 1,381.1</b>
Total debt	17.1	<b>16.9</b>
Working capital	1,460.1	<b>1,451.8</b>
Debt to total capitalization	0.7%	<b>0.7%</b>

Cash and cash equivalents increased in the first three months of fiscal 2004 as cash generated from operating activities and proceeds from the sales and maturities of short-term investments, sales of assets and proceeds from stock issuances exceeded the amount expended on capital assets, payment of dividends, and the repurchase of A