



*Roche Holdings, Inc.*  
*Annual Report 2010*

**Roche Holdings, Inc. Annual Report 2010**

**Management Report and**

**Consolidated Financial Statements**

**for the year ended on December 31, 2010**

# Management Report

## 1. Review of the twelve months ended December 31, 2010

### Important events

In 2010 the Roche Holdings, Inc. (RHI) Group achieved a solid operating performance. Sales increased by 1% to \$17.1 billion as the underlying growth of both the Pharmaceuticals and Diagnostics Division compensated for the expected decline in Tamiflu sales and the initial impacts of the U.S. healthcare reforms.

Effective March 26, 2009 the RHI Group obtained full ownership of Genentech, Inc. and substantially completed the relating integration and restructuring activities in 2010. Restructuring expenses of \$0.4 billion (2009: \$1.9 billion) were incurred.

In 2010, the RHI Group continued to pay down the debt which had been issued to finance the Genentech transaction. A total of \$8.2 billion of debt was repaid, which includes the early redemption of 2.5 billion of notes in September 2010. In addition, the RHI Group resolved to early redeem \$1.0 billion of notes maturing in March 2014. These notes will be redeemed on March 24, 2011.

On November 17, 2010 the Roche Group announced the details of its global 'Operational Excellence' program, which is a proactive and comprehensive initiative to reinforce the Roche Group's long-term innovation capability in the face of increased business challenges including pricing pressures in the United States and elsewhere. In the United States, implementation plans include reducing the work force by 3,550 positions and the main areas affected are in manufacturing, sales and marketing, product development as well as research and early development. This initiative is scheduled to be implemented in 2011 and 2012. Initial charges of \$0.4 billion were included in the 2010 results, mainly relating to employee severance costs and intangible asset impairments in the Pharmaceutical Division. Further disclosures are made in Note 7 to the Consolidated Financial Statements.

The effect of the U.S. healthcare reforms on the Pharmaceuticals Division in 2010 was a reduction in sales of \$0.25 billion.

Effective December 29, 2010 the Pharmaceuticals Division acquired the U.S. biopharmaceutical company Marcadia Biotech, Inc., ('Marcadia'), based in Carmel, Indiana. Marcadia is a biopharmaceutical company whose research programs focus on new peptide therapies for the treatment of metabolic diseases such as Type 2 diabetes and obesity. The total purchase consideration was \$377 million, of which \$287 million was paid in cash and \$90 million arises from a contingent consideration arrangement. The assets and liabilities and the amounts allocated to the purchase price are provisional based on preliminary information and valuations and are subject to adjustment during 2011, if new information is obtained about the facts and circumstances that existed at the acquisition date.

Effective September 3, 2010 the Diagnostics Division acquired the U.S. company Biomagene based in Sunnyvale, California. Biomagene is engaged in the digital pathology workflow and analysis. The acquisition complements and strengthens the RHI Group's portfolio in image analysis and information management. In 2010, there was another minor business combination in the Diagnostics Division. The total purchase consideration of these acquisitions was \$87 million in cash. Further disclosures are made in Note 6.

### Presentational changes

During 2010 the RHI Group has made certain presentational changes to the income statement, as commented in Note 1 to the Consolidated Financial Statements 2010. These have been made in light of current international and industry practice and taking into account the latest regulatory guidance. These changes have been applied retrospectively. The term 'exceptional items' is no longer used in the financial statements. Therefore, the term 'Operating profit before exceptional items' is deleted and income and expenses previously shown separately as 'Major legal cases' and 'Changes in RHI Group organization' are included as part of 'General and administration'. Likewise 'Exceptional financing costs' are included as part of 'Financial income' or 'Financing costs', as appropriate and 'Income taxes on exceptional items' are included as part of 'Income taxes'. Further disclosures are made in Notes 4, 5, 7 and 24 respectively.

## Financial performance

In 2010 the RHI Group's total sales increased by \$0.1 billion to \$17.1 billion, with the Pharmaceuticals Division representing 83% of total sales and the Diagnostics Division contributing 17%. Sales in the Pharmaceuticals Division remained stable at \$14.2 billion. There was strong growth in the key oncology products, especially Mabthera/Rituxan and Herceptin as well as Lucentis in ophthalmology. These increased sales were partly offset by the expected sharp decline in Tamiflu sales, the reduction in CellCept sales in transplantation due to the post-patent expiry in the United States in May 2009 and the initial impacts of the U.S. healthcare reforms. Pharmaceutical sales excluding Tamiflu increased 4%. The Diagnostics Division increased sales to \$2.9 billion in 2010, growing 5%. Major growth areas were Professional Diagnostics and Molecular Diagnostics.

The RHI Group's operating profit increased by \$2.3 billion to \$6.1 billion. The increase in profitability was driven by synergies from the Genentech integration, resource prioritization and further productivity improvements, despite the initial costs for the Operational Excellence program. The operating profit margin increased by 13.3 percentage points to reach 35.9%.

In the Pharmaceuticals Division the operating profit increased by \$2.2 billion to \$5.9 billion, driven primarily by synergies from the Genentech integration in all functions, higher positive effects of cost-sharing agreements with related parties and resource prioritization, notably in marketing and distribution, despite the initial costs for the Operational Excellence program of \$0.4 billion. Cost of sales decreased in comparison to 2009, as a result of lower royalty expenses and lower expenses for collaboration and profit-sharing agreements in 2010, further to an amended agreement with GlaxoSmithKline in the U.S. for Bonviva/Boniva. 2010 also includes the impacts of productivity improvements in technical operations, offset by unfavorable product mix effects. The comparative period includes the one-time impact of the inventory write-off for the voluntary withdrawal of Raptiva. Research and development costs, excluding intangible assets impairments, decreased by 4% mainly due to the positive impact of cost sharing agreements with related parties, resource prioritization and synergies. Research and development expenses also included the immediate recognition of the remaining costs of \$53 million necessary to cover the termination of the ocrelizumab rheumatoid arthritis development program and the payment received from Novartis for opting in the Lucentis study on the treatment of macular edema following retina/vein occlusion. The majority of the costs that were recorded as part of the Operational Excellence program relate to research and development. The \$0.3 billion costs in research and development related to impairments of intangible assets due to project terminations and to termination costs. General and administration costs in the Pharmaceuticals Division include \$0.4 billion of costs relating to employee-related costs and other reorganization expenses arising from the Genentech transaction (2009: \$1.9 billion).

The operating profit in the Diagnostics Division increased to \$0.2 billion. The operating profit margin improvement of 2.9 percentage points was driven by sales growth mainly in Professional Diagnostics and Molecular Diagnostics as well as higher royalty income. Furthermore, there was a favorable development of operating expenses, partly due to the non-recurrence of restructuring expenses recorded in 2009.

Overall this led to an increase of the RHI Group's operating profit to \$6.1 billion compared to \$3.8 billion in the same period of 2009.

In 2009, the RHI Group financed the Genentech transaction by a combination of own funds, bonds, notes and commercial paper. The RHI Group raised net proceeds of \$40.3 billion through a series of debt offerings. All newly issued debt is senior, unsecured and has been guaranteed by Roche Holding Ltd, the parent of the RHI Group. As a consequence, the underlying dynamics of the RHI Group's treasury results changed significantly, with a substantial increase in interest expenses. The reporting period of 2010 includes full twelve months of these interest expenses compared to only ten months in 2009. This effect was largely offset by lower interest expenses due to the debt repayments in 2009 and 2010. In addition the RHI Group incurred losses on early debt redemption of \$0.2 billion. Along with the bonds and notes issuances in 2009 the RHI Group entered into derivative contracts to hedge the foreign exchange risk arising from bonds and notes issued in currencies other than U.S. dollars. The losses on these derivative contracts are offset by foreign exchange gains on the bonds and notes issued in currencies other than U.S. dollars. The financing costs from related parties increased to \$1.0 billion mainly reflecting twelve months of financing costs in 2010 compared to only nine months in 2009 arising from the additional related-party debt taken on to fund the Genentech transaction. The RHI Group's effective tax rate increased to 37.4% from 13.1% in the comparative period, mainly due to a lower impact from U.S. research development and other manufacturing tax credits in 2010 compared to 2009 as well as the tax impact from equity compensation plans, which varies according to the price of the underlying equity. The impact from equity compensation plans on the effective tax rate 2010 was an increase of

1.8%, while in 2009 it was a benefit of 7.6%. This is mainly due to the one-time impact of the accelerated vesting of Genentech plans in 2009.

Overall net income increased by \$0.9 billion to \$2.1 billion. This increase primarily results from a strong operating performance in spite of significantly lower Tamiflu sales, as well as from strong cost containments despite initial charges from the Operational Excellence program. Charges incurred in respect of the Genentech transaction in 2010 compared to 2009 were significantly lower.

The cash flow from operating activities decreased by \$1.9 billion to \$6.2 billion. This is mainly a result of higher tax payments, as 2009 included the one-time \$0.9 billion tax benefit on the settlement of stock options with Genentech employees upon closing the transaction in March 2009. Cash from operating activities before tax payments decreased by \$0.8 billion, as higher cash generation from operations was more than offset principally by payments of certain large year-end 2009 accruals including the payment of the employee retention/severance schemes and high royalty payments relating to strong Tamiflu sales in the second half of 2009. The cash flow from investing activities decreased by \$6.6 billion as the comparative period contained \$7.3 billion proceeds from liquidation of certain debt securities to fund the Genentech transaction. The cash outflow from financing activities of \$5.3 billion was mainly due to the repayment of \$8.2 billion of notes as well as \$1.7 billion interest payments for the new debt issued in 2009, partly offset with a net inflow from related party financing of \$6.0 billion, including cash pool. The financing cash outflow of \$16.6 billion in 2009 included payments of \$47 billion for the Genentech transaction and proceeds of \$40.3 billion from issuance of bonds and notes. Furthermore, it included an outflow of \$2.9 billion into the Roche Group cash pool outside the United States. In 2010, the total decrease in cash was \$0.1 billion.

#### **Financial position**

The decrease in total assets mainly results from a decrease in related party receivables compared to December 31, 2009. The carrying value of debt, mainly from the financing of the Genentech transaction, at the end of 2010 was \$45.2 billion, compared to \$48.8 billion at the end of 2009. This reduction reflects the redemption on due dates in 2010 of the \$3 billion and 1.5 billion euro-denominated floating rate notes, the \$0.5 billion Genentech senior notes and the early redemption of notes on September 9, 2010 with a principal value of \$2.5 billion that were due March 1, 2012 as well as the decrease in the carrying value of the outstanding bonds denominated in foreign currencies due to the strengthening of the U.S. dollar. The decrease in bonds and notes was partly offset by an increase in related party debt of \$5.4 billion. In 2009 the Genentech transaction was accounted for in full as an equity transaction. As a consequence, the carrying amount of the consolidated equity of the RHI Group was significantly reduced. In 2010, the negative equity was reduced by \$2.2 billion to \$28.1 billion. The capacity of the RHI Group to generate positive cash flows and operating profit is not affected by this accounting treatment. In addition, bonds and notes with a carrying value of \$28.1 billion are guaranteed by Roche Holding Ltd, the parent company of the Roche Group.

## **2. Principal risks and uncertainties**

#### **Risks**

The RHI Group is exposed to various financial risks arising from its underlying operations and corporate finance activities. The RHI Group's financial risk exposures are predominantly related to changes in interest rates, equity prices and to an extent, foreign exchange rates, as well as the creditworthiness and the solvency of the RHI Group's counterparties. The RHI Group's financial risk management is described in Note 30 to the Consolidated Financial Statements for the year ended December 31, 2010.

#### **Uncertainties**

As well as being the holding company for the Roche Group's U.S. operations, a further activity of Roche Holdings, Inc. is to provide finance to other members of the RHI Group and to refinance this on the bond or loan markets.

The RHI Group's provisions and contingent liabilities are described in Note 24 to the Consolidated Financial Statements for the year ended December 31, 2010. In addition, key assumptions and sources of estimation uncertainty in the preparation of the financial statements are described in Note 1 to these Financial Statements.

The difficulties in the financial markets and the economy have had a limited impact on the RHI Group's businesses so far. The effect of the U.S. healthcare reforms in 2010 was \$0.25 billion, reducing sales in the Pharmaceuticals Division. However, the developments are being closely monitored, including credit risk from three major U.S. wholesalers that account for 65% of the RHI group's third party trade accounts receivable. As outlined above, the Operational

Excellence program announced on November 17, 2010 further aims at facing proactively and effectively external pressures.

Various known and unknown risks, uncertainties and other factors could lead to substantial differences between the future results, financial situation development or performance of the RHI Group and the historical results given in the Management Report and the Financial Statements for the year ended 2010.

### 3. Responsibility statement

The directors of Roche Holdings, Inc. confirm that, to the best of their knowledge as of the date of their approval of the audited consolidated financial statements as at January 26, 2011:

- the audited consolidated financial statements as at December 31, 2010, which have been prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of Roche Holdings, Inc. and the undertakings included in the consolidation taken as a whole and that
- the management report gives a true and fair view of the development and performance of the business and the position of Roche Holdings, Inc. and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

Franz B. Humer  
Chairman of the Board

Erich Hunziker  
Vice Chairman of the Board

Severin Schwan  
Member of the Board

Frank J. D'Angelo  
Member of the Board

Frederick C. Kentz III  
Member of the Board

David P. McDede  
Member of the Board

Bruce Resnick  
Member of the Board

# Roche Holdings, Inc. Consolidated Financial Statements

## Roche Holdings, Inc. consolidated income statement for the year ended December 31, 2010 in millions of USD

	Pharmaceuticals	Diagnostics	Corporate	RHI Group
<b>Sales</b> <sup>2</sup>	<b>14,178</b>	<b>2,920</b>	-	<b>17,098</b>
Royalties and other operating income <sup>2</sup>	<b>3,188</b>	<b>250</b>	-	<b>3,438</b>
Cost of sales	<b>(4,132)</b>	<b>(2,026)</b>	-	<b>(6,158)</b>
Marketing and distribution	<b>(2,103)</b>	<b>(672)</b>	-	<b>(2,775)</b>
Research and development <sup>2</sup>	<b>(4,008)</b>	<b>(142)</b>	-	<b>(4,150)</b>
General and administration	<b>(1,207)</b>	<b>(97)</b>	<b>(13)</b>	<b>(1,317)</b>
<b>Operating profit</b> <sup>2</sup>	<b>5,916</b>	<b>233</b>	<b>(13)</b>	<b>6,136</b>
Associates <sup>14</sup>				-
Financial income <sup>4</sup>				<b>261</b>
Financial income – related parties <sup>31</sup>				<b>55</b>
Financing costs <sup>4</sup>				<b>(2,098)</b>
Financing costs – related parties <sup>31</sup>				<b>(992)</b>
<b>Profit before taxes</b>				<b>3,362</b>
Income taxes <sup>5</sup>				<b>(1,258)</b>
<b>Net income</b>				<b>2,104</b>
Attributable to				
- Roche Holdings, Inc. shareholder				<b>2,104</b>

Reference numbers indicate corresponding Notes to the Consolidated Financial Statements.

**Roche Holdings, Inc. consolidated income statement for the year ended December 31, 2009** *in millions of USD*

	Pharmaceuticals	Diagnostics	Corporate	RHI Group
<b>Sales</b> <sup>2</sup>	<b>14,221</b>	<b>2,793</b>	-	<b>17,014</b>
Royalties and other operating income <sup>2</sup>	<b>3,236</b>	<b>221</b>	-	<b>3,457</b>
Cost of sales	<b>(4,335)</b>	<b>(1,939)</b>	-	<b>(6,274)</b>
Marketing and distribution	<b>(2,418)</b>	<b>(683)</b>	-	<b>(3,101)</b>
Research and development <sup>2</sup>	<b>(4,174)</b>	<b>(119)</b>	-	<b>(4,293)</b>
General and administration	<b>(2,803)</b>	<b>(130)</b>	<b>(23)</b>	<b>(2,956)</b>
<b>Operating profit</b> <sup>2</sup>	<b>3,727</b>	<b>143</b>	<b>(23)</b>	<b>3,847</b>
Associates <sup>14</sup>				-
Financial income <sup>4</sup>				<b>(724)</b>
Financial income – related parties <sup>31</sup>				<b>979</b>
Financing costs <sup>4</sup>				<b>(1,884)</b>
Financing costs – related parties <sup>31</sup>				<b>(848)</b>
<b>Profit before taxes</b>				<b>1,370</b>
Income taxes <sup>5</sup>				<b>(179)</b>
<b>Net income</b>				<b>1,191</b>
Attributable to				
- Roche Holdings, Inc. shareholder				<b>816</b>
- Non-controlling interests				<b>375</b>

As disclosed in Note 1, the income statement for 2009 has been restated following the accounting policy changes which were adopted in 2010. A reconciliation to the previously published income statement is provided in Note 1.



**Roche Holdings, Inc. consolidated statement of comprehensive income** *in millions of USD*

	Year ended December 31,	
	2010	2009
<b>Net income recognized in income statement</b>	<b>2,104</b>	1,191
<b>Other comprehensive income</b>		
Available-for-sale investments <sup>27</sup>	<b>(4)</b>	25
Cash flow hedges <sup>27</sup>	<b>(184)</b>	69
Defined benefit post-employment plans <sup>27</sup>	<b>13</b>	(5)
<b>Other comprehensive income, net of tax</b>	<b>(175)</b>	89
<b>Total comprehensive income</b>	<b>1,929</b>	1,280
Attributable to		
- Roche Holdings, Inc. shareholder <sup>27</sup>	<b>1,929</b>	890
- Non-controlling interests <sup>28</sup>	-	390
Total	<b>1,929</b>	1,280

**Roche Holdings, Inc. consolidated balance sheet** *in millions of USD*

	December 31, 2010	December 31, 2009	December 31, 2008
<b>Non-current assets</b>			
Property, plant and equipment <sup>11</sup>	6,205	6,274	7,615
Goodwill <sup>12</sup>	5,730	5,537	4,096
Intangible assets <sup>13</sup>	3,146	3,106	3,344
Associates <sup>14</sup>	-	-	-
Financial long-term assets <sup>15</sup>	112	130	371
Financial long-term assets – related parties <sup>31</sup>	89	95	95
Other long-term assets <sup>15</sup>	328	317	322
Other long-term assets – related parties <sup>31</sup>	338	169	-
Deferred income tax assets <sup>5</sup>	2,077	2,079	1,224
Post-employment benefit assets <sup>9</sup>	111	116	84
<b>Total non-current assets</b>	<b>18,136</b>	17,823	17,151
<b>Current assets</b>			
Inventories <sup>16</sup>	1,679	1,726	2,006
Accounts receivable – trade <sup>17</sup>	1,732	1,862	1,825
Accounts receivable – related parties <sup>23, 31</sup>	4,772	6,588	1,990
Current income tax assets <sup>5</sup>	39	101	103
Other current assets <sup>18</sup>	534	560	627
Marketable securities <sup>19</sup>	228	269	6,382
Cash and cash equivalents <sup>20</sup>	-	10	2,910
<b>Total current assets</b>	<b>8,984</b>	11,116	15,843
<b>Total assets</b>	<b>27,120</b>	28,939	32,994
<b>Non-current liabilities</b>			
Long-term debt <sup>26</sup>	(27,793)	(33,012)	(2,418)
Long-term debt – related parties <sup>26, 31</sup>	(10,080)	(8,400)	(7,612)
Deferred income tax liabilities <sup>5</sup>	(666)	(475)	(401)
Post-employment benefit liabilities <sup>9</sup>	(1,333)	(1,340)	(1,332)
Provisions <sup>24</sup>	(388)	(249)	(275)
Other non-current liabilities <sup>25</sup>	(88)	(116)	(151)
Other non-current liabilities – related parties <sup>31</sup>	(101)	(72)	-
<b>Total non-current liabilities</b>	<b>(40,449)</b>	(43,664)	(12,189)
<b>Current liabilities</b>			
Short-term debt <sup>26</sup>	(2,204)	(5,929)	(993)
Short-term debt – related parties <sup>26, 31</sup>	(5,135)	(1,415)	(205)
Current income tax liabilities <sup>5</sup>	(520)	(874)	(584)
Provisions <sup>24</sup>	(1,580)	(1,136)	(427)
Accounts payable – trade and other <sup>21</sup>	(533)	(622)	(526)
Accounts payable – related parties <sup>31</sup>	(891)	(993)	(747)
Accrued and other current liabilities <sup>22</sup>	(3,868)	(4,447)	(3,132)
Other current liabilities – related parties <sup>31</sup>	(86)	(156)	-
<b>Total current liabilities</b>	<b>(14,817)</b>	(15,572)	(6,614)
<b>Total liabilities</b>	<b>(55,266)</b>	(59,236)	(18,803)
<b>Total net assets</b>	<b>(28,146)</b>	(30,297)	14,191
<b>Equity</b>			
Capital and reserves attributable to Roche Holdings, Inc. shareholder <sup>27</sup>	(28,146)	(30,297)	7,200
Equity attributable to non-controlling interests <sup>28</sup>	-	-	6,991
<b>Total equity</b>	<b>(28,146)</b>	(30,297)	14,191

**Roche Holdings, Inc. consolidated statement of cash flows** *in millions of USD*

	Year ended December 31,	
	2010	2009
<b>Cash flows from operating activities</b>		
Cash generated from operations <sup>29</sup>	<b>8,781</b>	7,779
(Increase) decrease in working capital	<b>(790)</b>	631
(Increase) decrease in working capital related parties	<b>85</b>	421
Payments made for defined benefit post-employment plans <sup>9</sup>	<b>(25)</b>	(168)
Utilization of provisions <sup>24</sup>	<b>(520)</b>	(386)
Other operating cash flows	<b>(9)</b>	-
<b>Cash flows from operating activities, before income taxes paid</b>	<b>7,522</b>	8,277
Income taxes paid	<b>(1,372)</b>	(199)
<b>Total cash flows from operating activities</b>	<b>6,150</b>	8,078
<b>Cash flows from investing activities</b>		
Purchase of property, plant and equipment	<b>(651)</b>	(828)
Purchase of intangible assets	<b>(181)</b>	(164)
Disposal of property, plant and equipment	<b>23</b>	68
Disposal of intangible assets	<b>22</b>	123
Divestment of subsidiary <sup>33</sup>	-	27
Business combinations <sup>6</sup>	<b>(340)</b>	(30)
Interest received	<b>1</b>	59
Proceeds from repayment of loans issued to related parties	<b>7</b>	-
Interest received from related parties <sup>31</sup>	<b>9</b>	13
Sales of marketable securities	<b>150</b>	7,286
Purchases of marketable securities	-	(922)
Other investing cash flows	<b>19</b>	4
<b>Total cash flows from investing activities</b>	<b>(941)</b>	5,636
<b>Cash flows from financing activities</b>		
Proceeds from issue of bonds and notes <sup>26</sup>	-	40,304
Proceeds from issue of related party debt <sup>26</sup>	<b>11,165</b>	963
Redemption and repurchase of bonds and notes <sup>26</sup>	<b>(8,186)</b>	(7,222)
Repayment of related party debt <sup>26</sup>	<b>(5,765)</b>	(390)
Increase (decrease) in commercial paper <sup>26</sup>	<b>(83)</b>	(240)
Increase (decrease) in other debt	<b>(32)</b>	(91)
Hedging arrangements	<b>(19)</b>	33
Hedging arrangements related parties	<b>(156)</b>	1,422
Change in ownership interest in subsidiaries		
- Genentech <sup>3</sup>	-	(47,017)
- Memory <sup>6</sup>	-	(5)
Interest paid	<b>(1,694)</b>	(634)
Interests and other financing related parties <sup>31</sup>	<b>(928)</b>	(795)
Recharges and prepayments to related parties for equity compensation plans <sup>10</sup>	<b>(188)</b>	(178)
Genentech		
- Genentech equity compensation plans <sup>10</sup>	-	99
(Increase) decrease of cash pool balance with related parties <sup>31</sup>	<b>579</b>	(2,863)
<b>Total cash flows from financing activities</b>	<b>(5,307)</b>	(16,614)
<b>Increase (decrease) in cash and cash equivalents</b>	<b>(98)</b>	(2,900)
Cash and cash equivalents at January 1	<b>10</b>	2,910
<b>Cash and cash equivalents at December 31</b> <sup>a), 20</sup>	<b>(88)</b>	10

<sup>a)</sup> Cash overdrafts of \$88 million (2009: zero) are included within current liabilities in the balance sheet.

**Roche Holdings, Inc. consolidated statement of changes in equity** *in millions of USD*

	Share capital	Retained earnings	Fair value reserves	Hedging reserve	Total	Non-controlling interests	Total equity
<b>Year ended December 31, 2009</b>							
At January 1, 2009	1	7,127	65	7	7,200	6,991	14,191
Net income recognized in income statement	-	816	-	-	816	375	1,191
Available-for-sale investments	-	-	23	-	23	2	25
Cash flow hedges	-	-	-	56	56	13	69
Defined benefit post-employment plans	-	(5)	-	-	(5)	-	(5)
<b>Total comprehensive income</b>	-	<b>811</b>	<b>23</b>	<b>56</b>	<b>890</b>	<b>390</b>	<b>1,280</b>
Business combinations <sup>6</sup>	-	-	-	-	-	4	4
Capital contribution related parties <sup>27</sup>	-	382	-	-	382	-	382
Dividends <sup>27, 28</sup>	-	-	-	-	-	-	-
Equity compensation plans <sup>27, 28</sup>	-	297	-	-	297	154	451
Changes in ownership interests in subsidiaries							
- Genentech <sup>3</sup>	-	(39,050)	-	-	(39,050)	(7,550)	(46,600)
- Memory <sup>6</sup>	-	(1)	-	-	(1)	(4)	(5)
Changes in non-controlling interests <sup>27, 28</sup>	-	(15)	-	-	(15)	15	-
At December 31, 2009	1	(30,449)	88	63	(30,297)	-	(30,297)
<b>Year ended December 31, 2010</b>							
At January 1, 2010	<b>1</b>	<b>(30,449)</b>	<b>88</b>	<b>63</b>	<b>(30,297)</b>	-	<b>(30,297)</b>
Net income recognized in income statement	-	<b>2,104</b>	-	-	<b>2,104</b>	-	<b>2,104</b>
Available-for-sale investments	-	-	<b>(4)</b>	-	<b>(4)</b>	-	<b>(4)</b>
Cash flow hedges	-	-	-	<b>(184)</b>	<b>(184)</b>	-	<b>(184)</b>
Defined benefit post-employment plans	-	<b>13</b>	-	-	<b>13</b>	-	<b>13</b>
<b>Total comprehensive income</b>	-	<b>2,117</b>	<b>(4)</b>	<b>(184)</b>	<b>1,929</b>	-	<b>1,929</b>
Dividends <sup>27, 28</sup>	-	-	-	-	-	-	-
Equity compensation plans <sup>27, 28</sup>	-	<b>222</b>	-	-	<b>222</b>	-	<b>222</b>
Other movements	-	<b>(75)</b>	<b>53</b>	<b>22</b>	-	-	-
At December 31, 2010	<b>1</b>	<b>(28,185)</b>	<b>137</b>	<b>(99)</b>	<b>(28,146)</b>	-	<b>(28,146)</b>

# Notes to the Roche Holdings, Inc. Consolidated Financial Statements

Reference numbers indicate corresponding Notes to the Consolidated Financial Statements.

## 1. Summary of significant accounting policies

### **Basis of preparation of the consolidated financial statements**

These financial statements are the consolidated financial statements of Roche Holdings, Inc., a company incorporated in the State of Delaware, and its subsidiaries ('RHI' or 'the RHI Group'). RHI is 100% indirectly owned by Roche Holding Ltd, a public company registered in Switzerland and parent company of the Roche Group. Roche Holdings, Inc. and its subsidiaries are therefore members of the Roche Group.

The consolidated financial statements of the RHI Group have been prepared in accordance with International Financial Reporting Standards (IFRS). They have been prepared using the historical cost convention except that, as disclosed in the accounting policies below, certain items, including derivatives and available-for-sale investments, are shown at fair value. They were approved for issue by the Board of Directors on January 26, 2011.

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities at the date of the financial statements. If in the future such estimates and assumptions, which are based on management's best judgment at the date of the financial statements, deviate from the actual circumstances, the original estimates and assumptions will be modified as appropriate in the year in which the circumstances change.

Effective March 26, 2009, the purchase of the non-controlling interests in Genentech was completed (see Note 3). Based on the revised International Accounting Standard 27 'Consolidated and Separate Financial Statements' (IAS 27), which was adopted by RHI in 2008, this transaction was accounted for in full as an equity transaction. As a consequence, the carrying amount of the consolidated equity of the RHI Group was reduced by approximately \$47 billion and at December 31, 2010 the RHI Group had a negative equity of \$28.1 billion. The capacity of the RHI Group to generate positive cash flows and operating profit is not affected by this accounting treatment. In addition, bonds and notes with a carrying value of \$28.1 billion are guaranteed by Roche Holding Ltd, the parent company of the Roche Group. Accordingly, management has assessed that it remains appropriate to prepare the RHI Group's financial statements on a going concern basis. In 2010, the RHI Group generated an operating profit of \$6,136 million and a positive operating cash flow of \$6.2 billion.

Changes in accounting policies that arise from the application of new or revised standards and interpretations are applied retrospectively, unless otherwise specified in the transitional requirements of the particular standard or interpretation. Retrospective application requires that the results of the comparative period and the opening balances of that period are restated as if the new accounting policy had always been applied. In some cases the transitional requirements of the particular standard or interpretation specify that the changes are to be applied prospectively. Prospective application requires that the new accounting policy only be applied to the results of the current period and the comparative period is not restated. In addition comparatives have been reclassified or extended from the previously reported results to take into account any presentational changes.

### **Consolidation policy**

These financial statements are the consolidated financial statements of Roche Holdings, Inc., a company incorporated in the State of Delaware, and its subsidiaries.

The subsidiaries are those companies controlled, directly or indirectly, by Roche Holdings, Inc., where control is defined as the power to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. This control is normally evidenced when Roche Holdings, Inc. owns, either directly or indirectly, more than 50% of the voting rights or currently exercisable potential voting rights of a company's share capital. Special Purpose Entities are consolidated where the substance of the relationship is that the Special Purpose Entity is controlled by the RHI Group. Companies acquired during the year are consolidated from the date on which control is transferred to the RHI Group, and subsidiaries to be divested are included up to the date on which control passes from the RHI Group. Inter-company balances, transactions and resulting unrealized income are eliminated in full. Changes in ownership interests in subsidiaries are accounted for as equity transactions if they occur after control has already been obtained and if they do not result in a loss of control.

Investments in associates are accounted for using the equity method. These are companies over which the RHI Group exercises, or has the power to exercise, significant influence, but which it does not control. This is normally evidenced when the RHI Group owns 20% or more of the voting rights or currently exercisable potential voting rights of the company. Balances and transactions with associates that result in unrealized income are eliminated to the extent of the RHI Group's interest in the associate. Interests in joint ventures are reported using the line-by-line proportionate consolidation method.

### **Segment reporting**

The determination of the RHI Group's operating segments is based on the organization units for which information is reported to the RHI Group's management. The RHI Group has two divisions, Pharmaceuticals and Diagnostics. Revenues are primarily generated from the sale of prescription pharmaceutical products and diagnostic instruments, reagents and consumables, respectively. Both divisions also derive revenue from the sale or licensing of products or technology to third parties. Certain corporate activities that cannot be reasonably allocated to the other reportable business segments based on RHI's management and organizational structure are reported as 'Corporate'. Previously within the Pharmaceuticals Division there had been two sub-divisions, Roche Pharmaceuticals and Genentech. Following the completion of the Genentech transaction (see Note 3), the Genentech sub-division was merged into the Pharmaceuticals Division in these consolidated financial statements.

Transfer prices between operating segments are set on an arm's length basis. Operating assets and liabilities consist of property, plant and equipment, goodwill and intangible assets, trade receivables/payables, inventories and other assets and liabilities, such as provisions, which can be reasonably attributed to the reported operating segments. Non-operating assets and liabilities mainly include current and deferred income tax balances, post-employment benefit assets/liabilities and financial assets/liabilities such as cash, marketable securities, investments and debt.

### **Foreign currency translation**

RHI and its subsidiaries use the U.S. dollar as the functional and presentation currency. Local transactions in other currencies are initially reported using the exchange rate at the date of the transaction. Gains and losses from the settlement of such transactions and gains and losses on translation of monetary assets and liabilities denominated in other currencies are included in income, except qualifying cash flow hedges, which are recorded in equity.

### **Revenues**

Sales represent amounts received and receivable for goods supplied to customers after deducting trade discounts, cash discounts and volume rebates, and exclude sales taxes and other taxes directly linked to sales. Revenues from the sale of products are recognized upon transfer to the customer of significant risks and rewards. Trade discounts, cash discounts and volume rebates are recorded on an accrual basis consistent with the recognition of the related sales. Estimates of expected sales returns, charge-backs and other rebates, including Medicaid in the United States, are also deducted from sales and recorded as accrued liabilities or provisions or as a deduction from accounts receivable. Such estimates are based on analyses of existing contractual or legislatively mandated obligations, historical trends and RHI's experience. If the circumstances are such that the level of sales returns, and hence revenues, cannot be reliably measured, then sales are only recognized when the right of return expires, which is generally upon prescription of the products to patients. Other revenues are recorded as earned or as the services are performed. Where necessary, single transactions are split into separately identifiable components to reflect the substance of the transaction. Conversely, two or more transactions may be considered together for revenue recognition purposes, where the commercial effect cannot be understood without reference to the series of transactions as a whole.

### **Cost of sales**

Cost of sales includes the corresponding direct production costs and related production overheads of goods sold and services rendered. Royalties, alliance and collaboration expenses, including all collaboration profit-sharing arrangements are also reported as part of cost of sales. Start-up costs between validation and the achievement of normal production capacity are expensed as incurred.

### **Research and development**

Internal research costs are those costs incurred for the purpose of gaining new scientific or technical knowledge and understanding. These costs are expensed as incurred.

Internal development costs are those costs incurred for the application of research findings or other knowledge to plan and develop new products for commercial production. Such costs would qualify for capitalization as intangible assets only if all of the following criteria can be demonstrated:

- The technical feasibility of completing the development project successfully so that it will be available for use or sale.
- The intention to complete the development project.
- The ability to use or sell the results of the development project.
- That the development project would generate economic benefits. This would normally be evidenced by the existence and size of a market for the results of the project itself or the products that would result from the project.
- The availability of adequate technical, financial and other resources to complete the development project.
- The ability to measure the development expenditure reliably that would qualify for capitalization as an intangible asset.

The development projects undertaken by the RHI Group are subject to technical, regulatory and other uncertainties, such that, in the opinion of management, the criteria for capitalization are not met prior to obtaining marketing approval by the regulatory authorities in major markets. Internal development costs that do not meet these criteria are therefore expensed as incurred.

Post-marketing studies after regulatory approval, such as Phase IV costs in the pharmaceuticals business, are expensed as incurred. They generally involve safety surveillance and ongoing technical support of a drug after it receives marketing approval to be sold. They may be required by regulatory authorities or may be undertaken for safety or commercial reasons. The safety surveillance is designed to detect any rare or long-term adverse effects over a much larger patient population and longer time period than was possible during earlier stages of development. The costs of such post-marketing studies are not capitalized as intangible assets, as in the opinion of management, they do not generate separately identifiable incremental future economic benefits that can be reliably measured.

In addition to its internal research and development activities, the RHI Group is also party to in-licensing and similar arrangements with its alliance partners. The RHI Group may also acquire in-process research and development assets, either through business combinations or through purchases of specific assets.

In-process research and development resources acquired either through in-licensing arrangements, business combinations or separate purchases are capitalized as intangible assets if they are controlled by the RHI Group, are separately identifiable and are expected to generate future economic benefits, even if uncertainty exists as to whether the research and development will ultimately result in a marketable product. Consequently, upfront and milestone payments to third parties for pharmaceutical products or compounds before regulatory marketing approval are recognized as intangible assets. Assets acquired through such arrangements are measured on the basis set out below in the 'Intangible assets' policy and are reviewed for impairment as set out below in the 'Impairment of property, plant and equipment and intangible assets' policy. Once available for use, such intangible assets are amortized on a straight-line basis over the period of the expected benefit and are reviewed for impairment at each reporting date. If research and development are embedded in contracts for strategic alliances, the RHI Group carefully assesses whether upfront or milestone payments constitute funding of research and development work or acquisition of an asset.

### **Licensing, milestone and other upfront receipts**

Royalty income is recognized on an accrual basis in accordance with the substance of the respective licensing agreements. If the collectability of a royalty amount is not reasonably assured, those royalties are recognized as revenue when the cash is received. Certain RHI Group companies receive from third parties upfront, milestone and other similar payments relating to the sale or licensing of products or technology. Revenue associated with performance milestones is recognized based on achievement of the deliverables as defined in the respective agreements. Upfront payments and license fees for which there are subsequent deliverables are initially reported as deferred income and are recognized in income as earned over the period of the development collaboration or the manufacturing obligation.

### **Employee benefits**

Wages, salaries, social security contributions, paid annual leave and sick leave, bonuses, and non-monetary benefits are accrued in the year in which the associated services are rendered by employees of the RHI Group. Where the RHI Group provides long-term employee benefits, the cost is accrued to match the rendering of the services by the employees concerned. Liabilities for long-term employee benefits are discounted to take into account the time value of money, where material.

## **Pensions and other post-employment benefits**

Most employees are covered by defined benefit and defined contribution post-employment plans sponsored by RHI Group companies. RHI's contributions to defined contribution plans are charged to the appropriate income statement heading within the operating results in the year to which they relate. The accounting and reporting of defined benefit plans are based on recent actuarial valuations. The defined benefit obligations and service costs are calculated using the projected unit credit method. This reflects service rendered by employees to the dates of valuation and incorporates actuarial assumptions primarily regarding discount rates used in determining the present value of benefits, projected rates of remuneration growth and long-term expected rates of return for plan assets. Discount rates are based on the market yields of high-quality corporate bonds. Past service costs are allocated over the average period until the benefits become vested. Current and past service costs are charged to the appropriate income statement heading within the operating results. Pension plan administration and funding is overseen at a corporate level and any settlement gains and losses resulting from changes in funding arrangements are reported as general and administration expenses within the 'Corporate' segment. The expected returns on plan assets and interest costs are charged to financial income and financing costs, respectively. Actuarial gains and losses, which consist of differences between assumptions and actual experiences and the effects of changes in actuarial assumptions, are recorded directly in equity. Pension assets and liabilities in different defined benefit plans are not offset unless the RHI Group has a legally enforceable right to use the surplus in one plan to settle obligations in the other plan. The recognition of pension assets is limited to the total of the present value of any future refunds from the plans or reductions in future contributions to the plans and any cumulative unrecognized past service costs. Adjustments arising from the limit on the recognition of assets for defined benefit plans are recorded directly in equity.

## **Equity compensation plans**

Certain employees of the RHI Group participate in equity compensation plans, including separate plans at Genentech (prior to the Genentech transaction). The fair value of all equity compensation awards granted to employees is estimated at the grant date and recorded as an expense over the vesting period. The expense is charged to the appropriate income statement heading within the operating results. For equity-settled plans, an increase in equity is recorded for this expense and any subsequent cash flows from exercises of vested awards are recorded as changes in equity. For cash-settled plans, a liability is recorded, which is measured at fair value at each reporting date with any movements in fair value being recorded to the appropriate income statement heading within the operating results. Any subsequent cash flows from exercise of vested awards are recorded as a reduction of the liability.

## **Property, plant and equipment**

Property, plant and equipment are initially recorded at cost of purchase or construction, and include all costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. These include items such as costs of site preparation, installation and assembly costs and professional fees. The net costs of testing whether the asset is functioning properly, including validation costs, are also included in the initially recorded cost of construction. Interest and other borrowing costs incurred with respect to qualifying assets are capitalized and included in the carrying value of the assets.

Property, plant and equipment are depreciated on a straight-line basis, except for land, which is not depreciated. Estimated useful lives of major classes of depreciable assets are as follows:

Land improvements	40 years
Buildings	10-50 years
Machinery and equipment	5-15 years
Diagnostic instruments	3-5 years
Office equipment	3 years
Motor vehicles	5 years

Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate components. The estimated useful life of the assets is regularly reviewed and, if necessary, the future depreciation charge is accelerated. Repairs and maintenance costs are expensed as incurred.

## **Leases**

Where the RHI Group is the lessee, leases of property, plant and equipment where the RHI Group has substantially all of the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the start of the lease at fair value, or the present value of the minimum lease payments, if lower. The rental obligation, net of finance charges, is reported within debt. Assets acquired under finance leases are depreciated in accordance with RHI's policy



on property, plant and equipment. If there is no reasonable certainty that the RHI Group will obtain ownership by the end of the lease term, the asset is depreciated over the shorter of the lease term and its useful life. The interest element of the lease payment is charged against income over the lease term based on the effective interest rate method. Leases where substantially all of the risks and rewards of ownership are not transferred to the RHI Group are classified as operating leases. Payments made under operating leases are charged against income on a straight-line basis over the period of the lease.

Where the RHI Group is the lessor, which primarily occurs in the Diagnostics Division, assets subject to finance leases are initially reported as receivables at an amount equal to the net investment in the lease. Assets subject to operating leases are reported within property, plant and equipment. Lease income from finance leases is subsequently recognized as earned income over the term of the lease based on the effective interest rate method. Lease income from operating leases is recognized over the lease term on a straight-line basis.

### **Business combinations and goodwill**

Business combinations are accounted for using the acquisition method of accounting. The consideration transferred in a business combination is measured at fair value at the date of acquisition. This consideration includes the cash paid plus the fair value at the date of exchange of assets given, liabilities incurred or assumed and equity instruments issued by the RHI Group. The fair value of the consideration transferred also includes contingent consideration arrangements at fair value. Directly attributable acquisition-related costs are expensed in the current period and reported within general and administration expenses. At the date of acquisition the RHI Group recognizes the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquired business. The identifiable assets acquired and the liabilities assumed are initially recognized at fair value. Where the RHI Group does not acquire 100% ownership of the acquired business non-controlling interest are recorded as the proportion of the fair value of the acquired net assets attributable to the non-controlling interest. Goodwill is recorded as the surplus of the consideration transferred over the RHI Group's interest in the fair value of the acquired net assets. Any goodwill and fair value adjustments are recorded as assets and liabilities of the acquired business in the functional currency of that business. When the initial accounting for a business combination is incomplete at the end of a reporting period, provisional amounts are used. During the measurement period, the provisional amounts are retrospectively adjusted and additional assets and liabilities may be recognized, to reflect new information obtained about the facts and circumstances that existed at the acquisition date which would have affected the measurement of the amounts recognized at that date, had they been known. The measurement period does not exceed twelve months from the date of acquisition. Goodwill is not amortized, but is assessed for possible impairment at each reporting date and is additionally tested annually for impairment. Goodwill may also arise upon investments in associates, being the surplus of the cost of investment over the RHI Group's share of the fair value of the net identifiable assets. Such goodwill is recorded within investments in associates. Changes in ownership interests in subsidiaries are accounted for as equity transactions if they occur after control has already been obtained and if they do not result in a loss of control.

### **Intangible assets**

Purchased patents, licenses, trademarks and other intangible assets are initially recorded at cost. Where these assets have been acquired through a business combination, this will be the fair value allocated in the acquisition accounting. Intangible assets are amortized over their useful lives on a straight-line basis beginning from the point when they are available for use. Estimated useful life is the lower of the legal duration and the economic useful life. The estimated useful life of intangible assets is regularly reviewed.

### **Impairment of property, plant and equipment and intangible assets**

An impairment assessment is carried out when there is evidence that an asset may be impaired. In addition intangible assets that are not yet available for use are tested for impairment annually. When the recoverable amount of an asset, being the higher of its fair value less costs to sell and its value in use, is less than its carrying value, then the carrying value is reduced to its recoverable amount. This reduction is reported in the income statement as an impairment loss. Value in use is calculated using estimated cash flows, generally over a five-year period, with extrapolating projections for subsequent years. These are discounted using an appropriate long-term pre-tax interest rate. When an impairment loss arises, the useful life of the asset in question is reviewed and, if necessary, the future depreciation/amortization charge is accelerated. The impairment of financial assets is discussed below in the 'Financial assets' policy.

### **Impairment of goodwill**

Goodwill is assessed for possible impairment at each reporting date and is additionally tested annually for impairment. Goodwill is allocated to cash-generating units as described in Note 12. When the recoverable amount of the cash-generating unit, being the higher of its fair value less costs to sell or its value in use, is less than its carrying value, then

the carrying value of the goodwill is reduced to its recoverable amount. This reduction is reported in the income statement as an impairment loss. The methodology used in the impairment testing is further described in Note 12.

### **Inventories**

Inventories are stated at the lower of cost and net realizable value. The cost of finished goods and work in process includes raw materials, direct labor and other directly attributable costs and overheads based upon the normal capacity of production facilities. Cost is determined using the weighted average method. Net realizable value is the estimated selling price less cost to completion and selling expenses.

### **Accounts receivable**

Accounts receivable are carried at the original invoice amount less allowances made for doubtful accounts, trade discounts, cash discounts, volume rebates and similar allowances. An allowance for doubtful accounts is recorded for the difference between the carrying value and the recoverable amount where there is objective evidence that the RHI Group will not be able to collect all amounts due. Trade discounts, cash discounts, volume rebates and similar allowances are recorded on an accrual basis consistent with the recognition of the related sales, using estimates based on existing contractual obligations, historical trends and RHI's experience. Long-term accounts receivable are discounted to take into account the time value of money, where material.

### **Cash and cash equivalents**

Cash and cash equivalents include cash on hand and time, call and current balances with banks and similar institutions. Such balances are only reported as cash if they are readily convertible to known amounts of cash, are subject to insignificant risk of changes in value and have a maturity of three months or less from the date of acquisition. This definition is also used for the statement of cash flows. Cash overdrafts that are repayable on demand and form an integral part of the RHI Group's cash management are included as a component of cash and cash equivalents for the purpose of the consolidated statement of cash flows.

### **Provisions**

Provisions are recognized where a legal or constructive obligation has been incurred which will probably lead to an outflow of resources that can be reasonably estimated. In particular, restructuring provisions are recognized when the RHI Group has a detailed formal plan that has either commenced implementation or been announced. Provisions are recorded for the estimated ultimate liability that is expected to arise, taking into account the time value of money, where material. A contingent liability is disclosed where the existence of the obligation will only be confirmed by future events or where the amount of the obligation cannot be measured with reasonable reliability. Contingent assets are not recognized, but are disclosed where an inflow of economic benefits is probable.

### **Fair values**

Fair value is the amount for which a financial asset, liability or instrument could be exchanged between knowledgeable and willing parties in an arm's length transaction. It is determined by reference to quoted market prices or by the use of established valuation techniques such as option pricing models and the discounted cash flows method if quoted prices in an active market are not available ("fair value hierarchy"). Valuation techniques will incorporate observable market data about market conditions and other factors that are likely to affect the fair value of a financial instrument. Valuation techniques are typically used for derivative financial instruments. The fair values of financial assets and liabilities at the reporting date are not materially different from their reported carrying values unless specifically mentioned in the Notes to the Consolidated Financial Statements. Information on fair value hierarchy is included in Note 30 on risk management.

### **Financial assets**

Financial assets, principally investments, including marketable securities, are classified as either 'Fair-value-through-profit-or-loss', 'Available-for-sale', 'Held-to-maturity' or 'Loans and receivables'. Fair-value-through-profit-or-loss financial assets are either classified as held-for-trading or designated upon initial recognition. Held-for-trading financial assets are acquired principally to generate profit from short-term fluctuations in price. Financial assets are designated as fair-value-through-profit-or-loss if doing so results in more relevant information by eliminating a measurement or recognition inconsistency. Held-to-maturity financial assets are securities with a fixed maturity that the RHI Group has the intent and ability to hold until maturity. Loans and receivables are financial assets created by the RHI Group or acquired from the issuer in a primary market. They are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. All other financial assets are considered to be available-for-sale.

All financial assets are initially recorded at fair value, including transaction costs, except for assets at fair-value-through-profit-or-loss, which exclude transaction costs. All purchases and sales are recognized on the settlement date. Fair-value-through-profit-or-loss financial assets are subsequently carried at fair value, with all changes in fair value recorded as financial income in the period in which they arise. Held-to-maturity financial assets are subsequently carried at amortized cost using the effective interest rate method. Available-for-sale financial assets are subsequently carried at fair value, with all unrealized changes in fair value recorded in equity except for interest calculated using the effective interest rate method and foreign exchange components. When the available-for-sale financial assets are sold, impaired or otherwise disposed of, the cumulative gains and losses previously recognized in equity are included in financial income for the current period. Loans and receivables are subsequently carried at amortized cost using the effective interest rate method.

Financial assets are individually assessed for possible impairment at each reporting date. An impairment charge is recorded where there is objective evidence of impairment, such as where the issuer is in bankruptcy, default or other significant financial difficulty. In addition any available-for-sale equity securities that have a market value of more than 25% below their original cost, net of any previous impairment, will be considered as impaired. Any available-for-sale equity securities that have a market value below their original cost, net of any previous impairment, for a sustained six-month period will also be considered as impaired. Any decreases in the market price of less than 25% of original cost, net of any previous impairment, which are also for less than a sustained six-month period are not by themselves considered as objective evidence of impairment. Such movements in fair value are recorded in equity until there is objective evidence of impairment or until the asset is sold or otherwise disposed of. For financial assets carried at amortized cost, any impairment charge is the difference between the carrying value and the recoverable amount, calculated using estimated future cash flows discounted using the original effective interest rate. For available-for-sale financial assets, any impairment charge is the amount currently carried in equity for the difference between the original cost, net of any previous impairment, and the fair value. An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized. For debt securities measured at amortized cost or available-for-sale, the reversal is recognized in income. For equity securities held available-for-sale, the reversal is recognized directly in equity.

A financial asset is derecognized when the contractual cash flows from the asset expire or when the Group transfers the rights to receive the contractual cash flows from the financial assets in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognized as a separate asset or liability.

### **Derivatives**

Derivative financial instruments are initially recorded and subsequently carried at fair value. Apart from those derivatives designated as qualifying cash flow hedging instruments as discussed in the 'Hedging' policy below, all changes in fair value are recorded as financial income in the period in which they arise. Embedded derivatives are recognized separately if not closely related to the host contract and where the host contract is carried at amortized cost.

### **Hedge accounting**

For the purposes of hedge accounting, hedging relationships may be of three types. A 'fair value hedge' is a hedge of the exposure to changes in fair value of a recognized asset or liability, or an unrecognized firm commitment, or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect profit or loss. A 'cash flow hedge' is a hedge of the exposure to variability in cash flows that is attributable to a particular risk associated with a recognized asset or liability or a highly probable forecast transaction and could affect profit or loss. A 'hedge of a net investment in a foreign operation' is a hedge of the foreign currency exposure on a net investment in a foreign operation.

To qualify for hedge accounting the hedging relationship must meet several strict conditions on documentation, probability of occurrence (for cash flow hedges), hedge effectiveness and reliability of measurement. If these conditions are not met, then the relationship does not qualify for hedge accounting. In this case the hedging instrument and the hedged item are reported independently as if there were no hedging relationship. In particular any derivatives are reported at fair value, with changes in fair value included in financial income.

For qualifying fair value hedges, the hedging instrument is recorded at fair value and the hedged item is recorded at its previous carrying value, adjusted for any changes in fair value that are attributable to the hedged risk. Any changes in the fair values are reported in financial income.

For qualifying cash flow hedges, the hedging instrument is recorded at fair value. The portion of any change in fair value that is an effective hedge is included in equity, and any remaining ineffective portion is reported in financial income. If the hedging relationship is the hedge of the foreign currency risk of a firm commitment or highly probable forecasted transaction that results in the recognition of a non-financial asset or liability, the cumulative changes in the fair value of the hedging instrument that have been recorded in equity are included in the initial carrying value of the asset or liability at the date of recognition. For all other qualifying cash flow hedges, the cumulative changes in the fair value of the hedging instrument that have been recorded in equity are included in financial income when the forecasted transaction affects net income.

For qualifying hedges of net investment in a foreign entity, the hedging instrument is recorded at fair value. The portion of any change in fair value that is an effective hedge is included in equity. Any remaining ineffective portion is recorded in financial income where the hedging instrument is a derivative and in equity in other cases. If the entity is disposed of, then the cumulative changes of fair value of the hedging instrument that have been recorded in equity are reclassified to income.

## **Debt**

Debt instruments are initially recorded at cost, which is the proceeds received, net of transaction costs. Subsequently they are reported at amortized cost. Any discount between the net proceeds received and the principal value due on redemption is amortized over the duration of the debt instrument and is recognized as part of financing costs using the effective interest rate method. The Group derecognizes a financial liability when its contractual obligations are discharged, cancelled or expired.

Certain debt instruments have been designated as 'fair-value-through-profit-or-loss' where doing so results in more relevant information as it eliminates or significantly reduces measurement or recognition inconsistencies. Such debt instruments were reported at fair value, based on quoted prices in an active market, with movements in fair value reported within financial income. The Group's last such instrument was redeemed on July 6, 2009 as disclosed in Note 26.

## **Taxation**

Income taxes include all taxes based upon the taxable profits of the RHI Group, including withholding taxes payable on the distribution of retained earnings within the RHI Group. Other taxes not based on income, such as property and capital taxes, are included within general and administration expenses.

Liabilities for income taxes, mainly withholding taxes, which could arise on the remittance of retained earnings, principally relating to subsidiaries, are only recognized where it is probable that such earnings will be remitted in the foreseeable future.

Deferred income tax assets and liabilities are recognized on temporary differences between the tax bases of assets and liabilities and their carrying values in the financial statements. Deferred income tax assets relating to the carry-forward of unused tax losses are recognized to the extent that it is probable that future taxable profit will be available against which the unused tax losses can be utilized.

Current and deferred income tax assets and liabilities are offset when the income taxes are levied by the same taxation authority and when there is a legally enforceable right to offset them. Deferred income taxes are determined based on the currently enacted tax rates applicable in each tax jurisdiction where the RHI Group operates.

## **Discontinued businesses and non-current assets held for sale**

A discontinued business is a component of the RHI Group's business that represents a separate major line of business or is a subsidiary acquired exclusively with a view to resale. Reclassification as a discontinued business occurs upon disposal or when the operation meets the criteria to be classified as held for sale, if earlier.

A disposal group is a group of assets that are to be disposed of as a group in a single transaction, together with the liabilities directly associated with those assets that will be transferred in the transaction. The assets and liabilities in a disposal group are reclassified as held for sale if their value will be recovered principally through a sale rather than through continuing use. The disposal group must be available for sale in its current condition and the sale must be highly probable.

Immediately before classification as held for sale, the measurement of all assets and liabilities in a disposal group is updated in accordance with applicable accounting policies. Then, on initial classification as held for sale, disposal groups are recognized at the lower of carrying value and fair value less costs to sell. Impairment losses on initial classification as held for sale are included in the income statement.

### **Management judgments made in applying accounting policies**

The application of RHI's accounting policies may require management to make judgments, apart from those involving estimates, that can have a significant effect on the amounts recognized in the consolidated financial statements. Management judgment is particularly required when assessing the substance of transactions that have a complicated structure or legal form. These include, but are not limited to, the following areas:

**Revenue recognition:** The nature of RHI's business is such that many sales transactions do not have a simple structure. Sales agreements may consist of multiple components occurring at different times. RHI is also party to various out-licensing agreements, which can involve upfront and milestone payments that may occur over several years. These agreements may also involve certain future obligations. Revenue is only recognized when, in management's judgment, the significant risks and rewards of ownership have been transferred and when the RHI Group does not retain continuing managerial involvement or effective control over the goods sold or when the obligation has been fulfilled. For some transactions this can result in cash receipts being initially recognized as deferred income and then released to income over subsequent periods on the basis of the performance of the conditions specified in the agreement.

**Consolidation of subsidiaries and associates:** The RHI Group periodically undertakes transactions that may involve obtaining the right to control or significantly influence the operations of other companies. These transactions include the acquisition of all or part of the equity of other companies, the purchase of certain assets and assumption of certain liabilities and contingent liabilities of other companies, and entering into alliance agreements with other companies. Also included are transactions involving Special Purpose Entities and similar vehicles. In all such cases management makes an assessment as to whether the RHI Group has the right to control or significantly influence the other company's operations, and based on this assessment the other company is consolidated as a subsidiary or associated company. In making this assessment management considers the underlying economic substance of the transaction and not only the contractual terms.

**Business combinations:** Where the RHI Group acquires control of another business, the consideration transferred has to be allocated to the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquired business, with any residual recorded as goodwill. This process involves management making an assessment of the fair value of these items. Management judgment is particularly involved in the recognition and measurement of the following items:

- Intellectual property. This may include patents, licenses, trademarks and similar rights for currently marketed products and also the rights and scientific knowledge associated with projects that are currently in research or development phases.
- Contingencies such as legal and environmental matters.
- Contingent consideration arrangements.
- The recoverability of any accumulated tax losses previously incurred by the acquired company.

In all cases management makes an assessment based on the underlying economic substance of items concerned, and not only on the contractual terms, in order to fairly present these items.

**Leases:** The RHI Group is party to leasing arrangements, both as a lessee and as a lessor. The treatment of leasing transactions in the financial statements is mainly determined by whether the lease is considered to be an operating lease or a finance lease. In making this assessment, management looks at the substance of the lease, as well as the legal form, and makes a judgment about whether substantially all of the risks and rewards of ownership are transferred. Arrangements which do not take the legal form of a lease but that nevertheless convey the right to use an asset are also covered by such assessments.

### **Key assumptions and sources of estimation uncertainty**

The preparation of the consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income, expenses and related disclosures. The estimates and underlying assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for

making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Changes in accounting estimates may be necessary if there are changes in the circumstances on which the estimate was based, or as a result of new information or more experience. Such changes are recognized in the period in which the estimate is revised.

The key assumptions about the future and key sources of estimation uncertainty that have a significant risk of causing a material adjustment to the carrying value of assets and liabilities within the next twelve months are described below.

**Revenue recognition:** If the circumstances are such that the level of sales returns, and hence revenues, cannot be reliably measured, then sales are only recognized when the right of return expires, which is generally upon prescription of the products to patients. In order to estimate this, management uses publicly available information about prescriptions as well as information provided by wholesalers and other intermediaries.

**Sales allowances:** The RHI Group has provisions and accruals for expected sales returns, charge-backs and other rebates, including Medicaid in the United States, which at December 31, 2010 was \$977 million. Such estimates are based on analyses of existing contractual or legislatively-mandated obligations, historical trends and RHI's experience. Management believes that the total provisions and accruals for these items are adequate, based upon currently available information. As these deductions are based on management estimates, they may be subject to change as better information becomes available. Such changes that arise could impact the provisions and accruals recognized in the balance sheet in future periods and consequently the level of sales recognized in the income statement in future periods.

**Property, plant and equipment and intangible assets, including goodwill:** The RHI Group has property, plant and equipment with a carrying value of \$6,205 million as disclosed in Note 11. Goodwill has a carrying value of \$5,730 million (see Note 12) and intangible assets have a carrying value of \$3,146 million (see Note 13). All of these assets are reviewed annually for impairment as described above. To assess whether any impairment exists, estimates are made of the future cash flows expected to result from the use of the asset and its eventual disposal. Actual outcomes could vary significantly from such estimates of discounted future cash flows. Factors such as changes in the planned use of buildings, machinery or equipment, or closure of facilities, the presence or absence of competition, technical obsolescence or lower than anticipated sales of products with capitalized rights could result in shortened useful lives or impairment. Changes in the discount rates used could also lead to impairments.

**Pensions and other post-employment benefits:** Many of RHI's employees participate in post-employment defined benefit plans. The calculations of the recognized assets and liabilities from such plans are based upon statistical and actuarial calculations. In particular the present value of the defined benefit obligation is impacted by assumptions on discount rates used to arrive at the present value of future pension liabilities, and assumptions on future increases in salaries and benefits. Furthermore, RHI's independent actuaries use statistically based assumptions covering areas such as future withdrawals of participants from the plan and estimates of life expectancy. At December 31, 2010 the present value of RHI's defined benefit obligation is \$3,754 million for funded plans and \$418 million for unfunded plans (see Note 9). The actuarial assumptions used may differ materially from actual results due to changes in market and economic conditions, higher or lower withdrawal rates, longer or shorter life spans of participants, and other changes in the factors being assessed. These differences could impact the assets or liabilities recognized in the balance sheet in future periods.

**Legal provisions:** The RHI Group is party to various legal proceedings including claims arising from trade, and the most significant matters are described in Note 24. Legal provisions at December 31, 2010 total \$767 million. Management believes that the total provisions for legal proceedings are adequate based upon currently available information. However, given the inherent difficulties in estimating liabilities in this area, it cannot be guaranteed that additional costs will not be incurred beyond the amounts accrued. Additional claims could be made which might not be covered by existing provisions or by insurance. There can be no assurance that there will not be an increase in the scope of these matters or that any future lawsuits, claims, proceedings or investigations will not be material. Such changes that arise could impact the provisions recognized in the balance sheet in future periods.

**Environmental provisions:** The RHI Group has provisions for environmental remediation costs, which at December 31, 2010 total \$161 million, as disclosed in Note 24. The material components of the environmental provisions consist of costs to fully clean and refurbish contaminated sites, including landfills, and to treat and contain contamination at

certain other sites. Future remediation expenses are affected by a number of uncertainties that include, but are not limited to, the detection of previously unknown contaminated sites, the method and extent of remediation, the percentage of problematic materials attributable to the RHI Group at the remediation sites relative to that attributable to other parties, and the financial capabilities of the other potentially responsible parties. Management believes that the total provisions for environmental matters are adequate based upon currently available information. However, given the inherent difficulties in estimating liabilities in this area, it cannot be guaranteed that additional costs will not be incurred beyond the amounts accrued. The effect of the resolution of environmental matters on the results of operations cannot be predicted due to uncertainty concerning both the amount and the timing of future expenditures. Such changes that arise could impact the provisions recognized in the balance sheet in future periods.

**Income taxes:** At December 31, 2010 the net liability for current income taxes is \$481 million and the net asset for deferred income taxes is \$1,411 million, as disclosed in Note 5. Significant estimates are required to determine the current and deferred assets and liabilities for income taxes. Some of these estimates are based on interpretations of existing tax laws or regulations. Management believes that the estimates are reasonable and that the recognized liabilities for income tax-related uncertainties are adequate. Various internal and external factors may have favorable or unfavorable effects on the income tax assets and liabilities. These factors include, but are not limited to, changes in tax laws, regulations and/or rates, changing interpretations of existing tax laws or regulations, future levels of research and development spending and changes in overall levels of pre-tax earnings. Such changes that arise could impact the assets and liabilities recognized in the balance sheet in future periods.

## Changes in accounting policies

In 2008 the RHI Group early adopted the revised versions of IFRS 3 'Business Combinations', IAS 27 'Consolidated and Separate Financial Statements' which were required to be implemented from January 1, 2010 at the latest. In 2010 the RHI Group implemented various amendments to existing standards and interpretations, which have no material impact on the RHI Group's overall results and financial position.

**Presentation of income statement:** During 2010 the RHI Group has made certain presentational changes to the income statement. These have been made in light of current international and industry practice and taking into account the latest regulatory guidance. These changes, which have been applied retrospectively, are listed below:

- The term 'exceptional items' is no longer used in the financial statements.
- The income statement headings 'Major legal cases' and 'Changes in RHI Group organization' are no longer shown separately on the face of the income statement. Such income and expenses are included as part of 'General and administration'. Disclosure is made in Notes 24 and 7 respectively.
- The sub-total for 'Operating profit before exceptional items' is deleted as it is redundant.
- The income statement heading 'Exceptional financing costs' is no longer shown separately on the face of the income statement. Such income and expenses are included as part of 'Financial income' or 'Financing costs', as appropriate. Disclosure is made in Note 4.
- The income statement heading 'Income taxes on exceptional items' is no longer shown separately on the face of the income statement. Such income and expenses are included as part of 'Income taxes'. Disclosure is made in Note 5.

The income statement for the year ended December 31, 2009 has been restated following the above changes as set out in the table below.

### Restated consolidated income statement for the year ended 31 December 2009 *in millions of USD*

	As originally published	Reclassifications	Restated
<b>Sales</b>	17,014	-	17,014
Royalties and other operating income	3,457	-	3,457
Cost of sales	(6,274)	-	(6,274)
Marketing and distribution	(3,101)	-	(3,101)
Research and development	(4,293)	-	(4,293)
General and administration	(811)	(2,145)	(2,956)
Major legal cases	(295)	295	-
Changes in RHI Group organization	(1,850)	1,850	-
<b>Operating profit</b>	<b>3,847</b>	<b>-</b>	<b>3,847</b>
Associates	-	-	-
Financial income	(694)	(30)	(724)
Financial income – related parties	979	-	979
Financing costs	(1,760)	(124)	(1,884)
Financing costs – related parties	(848)	-	(848)
Exceptional financing costs	(154)	154	-
<b>Profit before taxes</b>	<b>1,370</b>	<b>-</b>	<b>1,370</b>
Income taxes	(1,154)	975	(179)
Income taxes on exceptional items	975	(975)	-
<b>Net income</b>	<b>1,191</b>	<b>-</b>	<b>1,191</b>

The RHI Group is currently assessing the potential impacts of the other new and revised standards and interpretations that will be effective from January 1, 2011 and beyond, and which the RHI Group has not early adopted. The RHI Group does not anticipate that these will have a material impact on the RHI Group's overall results and financial position.



## 2. Operating segment information

### **Divisional information** *in millions of USD*

	Pharmaceuticals		Diagnostics		Corporate		RHI Group	
	2010	2009	2010	2009	2010	2009	2010	2009
<b>Revenues from external customers and related parties</b>								
Sales	<b>14,178</b>	14,221	<b>2,920</b>	2,793	-	-	<b>17,098</b>	17,014
Royalties and other operating income	<b>3,188</b>	3,236	<b>250</b>	221	-	-	<b>3,438</b>	3,457
<b>Total</b>	<b>17,366</b>	17,457	<b>3,170</b>	3,014	-	-	<b>20,536</b>	20,471
<b>Segment results</b>								
Operating profit	<b>5,916</b>	3,727	<b>233</b>	143	<b>(13)</b>	(23)	<b>6,136</b>	3,847
<b>Capital expenditure</b>								
Business combinations	<b>451</b>	54	<b>113</b>	-	-	-	<b>564</b>	54
Additions to property, plant and equipment	<b>490</b>	595	<b>154</b>	203	-	-	<b>644</b>	798
Additions to intangible assets	<b>176</b>	164	<b>5</b>	-	-	-	<b>181</b>	164
<b>Total capital expenditure</b>	<b>1,117</b>	813	<b>272</b>	203	-	-	<b>1,389</b>	1,016
<b>Research and development</b>								
Research and development costs	<b>4,008</b>	4,174	<b>142</b>	119	-	-	<b>4,150</b>	4,293
<b>Other segment information</b>								
Depreciation of property, plant and equipment	<b>490</b>	599	<b>143</b>	129	-	-	<b>633</b>	728
Amortization of intangible assets	<b>69</b>	123	<b>177</b>	181	-	-	<b>246</b>	304
Impairment of property, plant and equipment	<b>57</b>	858	<b>2</b>	3	-	-	<b>59</b>	861
Impairment of goodwill	-	-	-	-	-	-	-	-
Impairment of intangible assets	<b>227</b>	427	<b>16</b>	36	-	-	<b>243</b>	463
Equity compensation plan expenses	<b>172</b>	409	<b>20</b>	24	<b>2</b>	3	<b>194</b>	436

**Net operating assets** *in millions of USD*

	Assets			Liabilities			Net assets		
	2010	2009	2008	2010	2009	2008	2010	2009	2008
Pharmaceuticals	<b>12,877</b>	13,004	15,212	<b>(5,140)</b>	(5,423)	(3,969)	<b>7,737</b>	7,581	11,243
Diagnostics	<b>7,481</b>	7,449	6,147	<b>(868)</b>	(766)	(853)	<b>6,613</b>	6,683	5,294
Corporate	<b>7</b>	170	409	<b>(43)</b>	(203)	(347)	<b>(36)</b>	(33)	62
Total operating	<b>20,365</b>	20,623	21,768	<b>(6,051)</b>	(6,392)	(5,169)	<b>14,314</b>	14,231	16,599
Non-operating	<b>6,755</b>	8,316	11,226	<b>(49,215)</b>	(52,844)	(13,634)	<b>(42,460)</b>	(44,528)	(2,408)
RHI Group	<b>27,120</b>	28,939	32,994	<b>(55,266)</b>	(59,236)	(18,803)	<b>(28,146)</b>	(30,297)	14,191

Supplementary information on sales for major products is given on page 3 of the Management Report.

**Major customers**

Substantially all of the RHI Group's third party sales are to customers in the United States. The U.S. national wholesale distributors, AmerisourceBergen Corp., Cardinal Health, Inc. and McKesson Corp. each contributed more than 10% of the RHI Group's revenues. The total amounts of revenues are approximately \$6 billion (2009: \$6 billion), \$3 billion (2009: \$3 billion) and \$4 billion (2009: \$4 billion), respectively. These revenues arose primarily in the Pharmaceuticals segment.

### 3. Genentech

Effective September 7, 1990 the RHI Group acquired a majority interest of approximately 60% of Genentech, Inc., a biotechnology company in the United States. The common stock of Genentech was publicly traded and was listed on the New York Stock Exchange, under the symbol 'DNA'. At December 31, 2008 RHI's interest in Genentech was 55.8%.

#### **Genentech transaction**

On March 12, 2009, Roche entered into a merger agreement with Genentech pursuant to which the Group made a successful tender offer to purchase all of the shares of Genentech not already owned by the Group for \$95.00 per share in cash (the 'Genentech transaction'). As a result, Genentech became a wholly-owned subsidiary of the RHI Group, effective March 26, 2009.

The cash consideration for the purchase of all public shares, including shares issuable under Genentech's outstanding employee stock options and payment of related fees and expenses, amounted to approximately \$47 billion, as set out in the table below. These amounts have been recorded to equity as a change in ownership interest in subsidiaries.

#### **Genentech transaction – 2009** *in millions of USD*

Purchase of publicly held shares	44,400
Settlement of outstanding employee stock options	2,412
Directly attributable transaction costs	205
Total cash consideration	<b>47,017</b>
Income tax effects	(417)
Change in ownership interest in subsidiaries	<b>46,600</b>

The RHI Group financed the Genentech transaction by a combination of the RHI Group's own funds, bonds, notes and commercial paper. The RHI Group raised net proceeds of \$40.3 billion through a series of debt offerings, as described in Note 26. All newly issued debt is senior, unsecured and has been guaranteed by Roche Holding Ltd., the parent of the RHI Group.

The impacts of the Genentech transaction and the related reorganization of the Roche's Pharmaceuticals business on the RHI Group's results are described in Note 7.

#### 4. Financial income and financing costs

##### **Financial income** *in millions of USD*

	Year ended December 31,	
	2010	2009
Gains on sale of equity securities	<b>100</b>	29
(Losses) on sale of equity securities	-	(1)
Write-downs and impairments of equity securities	<b>(2)</b>	(4)
Net income from equity securities	<b>98</b>	24
Interest income	<b>1</b>	58
Gain (loss) on liquidation of debt securities	-	(30)
Net interest income and income from debt securities	<b>1</b>	28
Expected return on plan assets of defined benefit plans <sup>9</sup>	<b>209</b>	184
Foreign exchange gains (losses), net	<b>(54)</b>	(966)
Gains (losses) on foreign currency derivatives, net	-	-
Net foreign exchange (losses)	<b>(54)</b>	(966)
Net other financial income (expense)	<b>7</b>	6
Total financial income	<b>261</b>	(724)

Net foreign exchange losses of \$54 million were largely offset by a net gain of \$46 made on foreign exchange forward contracts with related parties (see Note 31). The related party derivatives mirror exactly the terms of derivative contracts that a Roche Group affiliate outside the RHI Group has entered with third party financial institutions.

##### **Financing costs** *in millions of USD*

	Year ended December 31,	
	2010	2009
Interest expense	<b>(1,573)</b>	(1,485)
Interest expense incurred on newly issued bonds and notes during bridging period	-	(124)
Amortization of debt discount <sup>26</sup>	<b>(43)</b>	(41)
Gains (losses) on debt derivatives, net	-	2
Gains (losses) on redemption and repurchase of bonds and notes, net <sup>26</sup>	<b>(244)</b>	(8)
Gains (losses) on financial liabilities at fair-value-through-profit-or-loss, net	-	6
Time cost of provisions <sup>24</sup>	<b>(16)</b>	(17)
Interest cost of defined benefit plans <sup>9</sup>	<b>(222)</b>	(217)
Total financing costs	<b>(2,098)</b>	(1,884)

##### **Net financial income** *in millions of USD*

	Year ended December 31,	
	2010	2009
Financial income	<b>261</b>	(724)
Financing costs	<b>(2,098)</b>	(1,884)
Net financial income	<b>(1,837)</b>	(2,608)
Financial result from Treasury management	<b>(1,824)</b>	(2,575)
Financial result from Pension management	<b>(13)</b>	(33)
Net financial income	<b>(1,837)</b>	(2,608)

**Genentech transaction financing costs:** As described in Note 3, effective March 26, 2009 the RHI Group purchased all publicly owned shares of Genentech for \$95.00 per share in cash, with the total cash consideration of the transaction, including shares issuable under Genentech's outstanding employee stock option plans and payment of related fees and expenses, being approximately \$47.0 billion.

In order to execute this transaction, Roche's Treasury operations liquidated certain debt securities into cash. This resulted in a net loss on these transactions of \$30 million. Furthermore, due to the prevailing financial conditions, the RHI Group issued bonds and notes in advance of the transaction totaling \$40.3 billion through a series of debt offerings,

as described in Note 26. The interest expense on these instruments for the bridging period between their issue and the completion of the Genentech transaction on March 26, 2009 was \$124 million.

These were previously presented as 'Exceptional financial costs'. As disclosed in Note 1, such income and expenses are no longer shown separately on the face of the income statement, but are now included as part of 'Financial income' or 'Financing costs', as appropriate. Appropriate reclassifications have been made to the 2009 disclosures in this Note.

## 5. Income taxes

### **Income tax expenses** *in millions of USD*

	2010	2009
Current income taxes	<b>(1,123)</b>	(1,676)
Adjustments recognized for current tax of prior periods	<b>23</b>	114
Deferred income taxes	<b>(158)</b>	1,383
Total income (expense)	<b>(1,258)</b>	(179)

As disclosed in Note 1, the income statement heading 'Income taxes on exceptional items' is no longer shown separately on the face of the income statement. Such income and expenses are included as part of 'Income taxes'. Appropriate reclassifications have been made to the 2009 disclosures in this Note, including restatement of the reconciliation of the RHI's effective tax rate in the table below.

RHI's effective tax rate can be reconciled to the RHI Group's average expected tax rate as follows:

### **Reconciliation of RHI's effective tax rate**

	2010	2009
Average expected tax rate	<b>35.0%</b>	35.0%
Tax effect of		
- Non-taxable income/non-deductible expenses	<b>+0.2%</b>	+0.1%
- Equity compensation plans	<b>+1.8%</b>	-7.6%
- Research, development and other manufacturing tax credits	<b>-6.2%</b>	-16.9%
- U.S. state tax impacts	<b>+4.5%</b>	+3.1%
- Other differences	<b>+2.1%</b>	-0.6%
RHI's effective tax rate	<b>37.4%</b>	13.1%

The impact from equity compensation plans on the effective tax rate 2010 was an increase of 1.8%, while in 2009 it was a benefit of 7.6%. This is mainly due to the one-time impact of the accelerated vesting of Genentech plans in 2009. The lower impact from U.S. research, development and other manufacturing tax credits in 2010 also increased the RHI Group effective tax rate compared to 2009.

### **Tax effects of other comprehensive income** *in millions of USD*

	2010			2009		
	Pre-tax amount	Tax benefit	After-tax amount	Pre-tax amount	Tax benefit	After-tax amount
Available-for-sale investments	<b>(8)</b>	<b>4</b>	<b>(4)</b>	34	(9)	25
Cash flow hedges	<b>(287)</b>	<b>103</b>	<b>(184)</b>	107	(38)	69
Defined benefit post-employment plans	<b>20</b>	<b>(7)</b>	<b>13</b>	(43)	38	(5)
Other comprehensive income	<b>(275)</b>	<b>100</b>	<b>(175)</b>	98	(9)	89

**Income tax assets (liabilities) in millions of USD**

	2010	2009	2008
Current income taxes			
- Assets	<b>39</b>	101	103
- Liabilities	<b>(520)</b>	(874)	(584)
Net current income tax assets (liabilities)	<b>(481)</b>	(773)	(481)
Deferred income taxes			
- Assets	<b>2,077</b>	2,079	1,224
- Liabilities	<b>(666)</b>	(475)	(401)
Net deferred income tax assets (liabilities)	<b>1,411</b>	1,604	823

Movements in amounts recorded on the balance sheet for current income taxes are shown in the table below:

**Current income taxes: movements in recognized net assets (liabilities) in millions of USD**

	2010	2009
Net current income tax asset (liability) at 1 January	<b>(773)</b>	(481)
Income taxes paid	<b>1,372</b>	199
(Charged) credited to the income statement		
- Current income taxes	<b>(1,123)</b>	(1,676)
- Adjustments recognized for current tax of prior periods	<b>23</b>	114
(Charged) credited to equity from equity compensation plans and other transactions with shareholders	<b>15</b>	1,085
Other	<b>5</b>	(14)
Net current income tax asset (liability) at December 31	<b>(481)</b>	(773)

Deferred income tax assets are recognized for tax loss carry-forwards only to the extent that realization of the related tax benefit is probable. The RHI Group has unrecognized tax losses, including valuation allowances, as follows:

**Unrecognized tax losses: expiry**

	Amount (mUSD)	2010 Applicable tax rate	Amount (mUSD)	2009 Applicable tax rate
Within one year	-	-	-	-
Between one and five years	-	-	-	-
More than five years	<b>923</b>	<b>4%</b>	115	35%
Total unrecognized tax losses	<b>923</b>	<b>4%</b>	115	35%

The 'More than five' years category includes losses that cannot be used for U.S. state income tax purposes in those states which only permit tax reporting on a separate entity basis.

Deferred income tax liabilities have not been established for the withholding tax and other taxes that would be payable on the unremitted earnings, as such amounts are currently regarded as permanently reinvested. These unremitted earnings totaled \$5.1 billion at 31 December 2010 (2009: none).

Movements in amounts recorded on the balance sheet for deferred income taxes are shown in the table below:

**Deferred income taxes: movements in recognized net assets (liabilities) in millions of USD**

	Property, plant and equipment, and intangible assets	Other temporary differences	Total
<b>Year ended December 31, 2009</b>			
Net deferred income tax asset (liability) at January 1, 2009	(1,321)	2,144	823
Memory acquisition <sup>6</sup>	(16)	21	5
(Charged) credited to the income statement	328	1,055	1,383
(Charged) credited to equity from other comprehensive income <sup>27</sup>	-	(9)	(9)
(Charged) credited to equity from equity compensation plans and other transactions with shareholders	-	(460)	(460)
Other	(153)	15	(138)
Net deferred income tax asset (liability) at December 31, 2009	(1,162)	2,766	1,604

**Year ended December 31, 2010**

Net deferred income tax asset (liability) at January 1, 2010	(1,162)	2,766	1,604
Marcadia acquisition <sup>6</sup>	(120)	8	(112)
Other business combinations <sup>6</sup>	(28)	23	(5)
(Charged) credited to the income statement	27	(185)	(158)
(Charged) credited to equity from other comprehensive income <sup>27</sup>	-	100	100
(Charged) credited to equity from equity compensation plans and other transactions with shareholders	-	(18)	(18)
Net deferred income tax asset (liability) at December 31, 2010	(1,283)	2,694	1,411

**6. Business combinations****Acquisitions – 2010**

Effective December 29, 2010 the RHI Group acquired a 100% controlling interest in Marcadia Biotech, Inc., ('Marcadia'), a privately owned U.S. company based in Carmel, Indiana. Marcadia is a biopharmaceutical company focused on developing a broad portfolio of drug candidates for the treatment of diabetes and obesity. Marcadia is now reported as part of the Pharmaceuticals operating segment. The acquisition of Marcadia will allow the RHI Group to integrate Marcadia's development pipeline into its own Research and Development portfolio. Marcadia's research programs focus on new peptide therapies for the treatment of Type 2 diabetes and obesity. These include next generation peptides such as MAR701, a novel compound currently in Phase I development. Based on Marcadia's unique peptide chemistry technology, these peptides are designed to offer patients improved efficacy, safety and convenience.

The total purchase consideration was \$377 million, of which \$287 million was paid in cash and \$90 million arises from a contingent consideration arrangement. The payment from this arrangement is based on the achievement of two separate performance milestones that may arise between 2013 and 2015 and the range of outcomes, undiscounted, is between zero and \$250 million. A liability of \$90 million was recognized at the acquisition date, based on management's best estimate of the probability-adjusted expected cash outflow from the arrangement. As at December 31, 2010 the amount recognized for this arrangement was unchanged, based on the most recent management estimates.

The purchase has been allocated as shown in the table below. The assets and liabilities and the amounts allocated to them are provisional based on preliminary information and valuations of the assets and liabilities of Marcadia. They are subject to adjustment during 2011, if new information is obtained about the facts and circumstances that existed at the acquisition date.

**Marcadia acquisition: net assets acquired in millions of USD**

	Carrying value prior to acquisition	Fair value adjustments	Carrying value upon acquisition
Intangible assets			
- Product intangibles: in use	-	93	93
- Product intangibles: not available for use	-	206	206
Inventories	-	-	-
Deferred income taxes	10	(122)	(112)
Cash	34	-	34
Other net assets (liabilities)	4	-	4
Net identifiable assets	48	177	225
Goodwill			152
Purchase consideration			377

Goodwill represents a control premium and synergies that can be obtained from the Group's existing business. None of the goodwill recognized is expected to be deductible for income tax purposes.

The fair value of other net assets (liabilities) includes receivables with a fair value of \$6 million.

**Other acquisitions:** Effective September 3, 2010 the RHI Group acquired a 100% controlling interest in Biolmagene, Inc., ('Biolmagene'), a privately owned U.S. company, based in Sunnyvale, California. Biolmagene is engaged in the digital pathology workflow and analysis field and is reported as part of the Diagnostics operating segment. The

acquisition complements and strengthens the RHI Group's portfolio in image analysis and diagnosis. The total purchase consideration was \$85 million in cash.

There was another minor business combination in the Diagnostics business with a total purchase consideration of \$2 million in cash.

The combined purchase consideration has been allocated as follows:

**Other acquisitions - 2010: net assets acquired** *in millions of USD*

	Carrying value prior to acquisition	Fair value adjustments	Carrying value upon acquisition
Property, plant and equipment	1	-	1
Goodwill	-	-	-
Intangible assets			
- Product intangibles: in use	-	17	17
- Product intangibles: not available for use	-	51	51
- Technology intangibles: in use	-	3	3
Inventories	2	-	2
Deferred income taxes	-	(5)	(5)
Cash	-	-	-
Other net assets (liabilities)	(23)	-	(23)
Net identifiable assets (liabilities)	(20)	66	46
Goodwill			41
Purchase consideration			87

Goodwill represents a control premium and synergies that can be obtained from the Group's existing business. None of the goodwill recognized is expected to be deductible for income tax purposes.

The fair value of other net assets (liabilities) does not include any receivables.

Directly attributable transaction costs of \$2 million were incurred in these acquisitions. These are reported within general and administration expenses in the current period as part of the operating result of the Pharmaceuticals and Diagnostics operating segment (\$1 million each).

**Acquisitions - 2010: impact on results** *in millions of USD*

	Revenues from external customers	Inventory fair value adjustment	Amortisation of intangible assets	Operating profit	Net income
<b>Impact on reported results</b>					
Marcadia	-	-	-	-	-
Pharmaceuticals Division	-	-	-	-	-
Biolmagene	1	-	(1)	(6)	(4)
Minor business combination	-	-	-	-	-
Diagnostics Division	1	-	(1)	(6)	(4)
RHI Group	1	-	(1)	(6)	(4)
<b>Estimated impact on results if acquisition assumed effective January 1, 2010</b>					
Marcadia	20	-	(9)	(1)	-
Pharmaceuticals Division	20	-	(9)	(1)	-
Biolmagene	2	-	(1)	(19)	(12)
Minor business combination	-	-	(1)	(2)	(1)
Diagnostics Division	2	-	(2)	(21)	(13)
RHI Group	22	-	(11)	(22)	(13)



The above figures exclude directly attributable acquisition-related costs of \$1 million related to acquisitions by the Pharmaceuticals Division and \$1 million related to acquisitions by the Diagnostics Division. Corresponding tax impacts are also excluded.

a) The figures exclude integration costs of \$2 million related to Marcadia and Biologics. Corresponding tax impacts are also excluded.

**Acquisitions – 2010: net cash outflow** *in millions of USD*

	Cash consideration paid	Cash in acquired company	Net cash outflow
Marcadia	<b>(287)</b>	<b>34</b>	<b>(253)</b>
Other acquisitions	<b>(87)</b>	-	<b>(87)</b>
Total acquisitions	<b>(374)</b>	<b>34</b>	<b>(340)</b>

**Acquisitions – 2009**

Effective January 1, 2009 the RHI Group acquired an 89.6% controlling interest in Memory Pharmaceuticals Corp. ('Memory'), a publicly owned U.S. company based in Montvale, New Jersey, that had been listed on the NASDAQ under the symbol 'MEMY'. Memory develops innovative drug candidates for the treatment of debilitating central nervous system (CNS) disorders such as Alzheimer's disease and schizophrenia. Memory is reported as part of the Pharmaceuticals operating segment. The acquisition will further strengthen the RHI Group's research and development pipeline in areas such as Alzheimer's disease. The purchase consideration was \$45 million, paid in cash.

The purchase consideration has been allocated as follows:

**Memory acquisition: net assets acquired** *in millions of USD*

	Carrying value prior to acquisition	Fair value adjustments	Carrying value upon acquisition
Intangible assets			
- Product intangibles: not available for use	-	<b>44</b>	<b>44</b>
Deferred income taxes <sup>5</sup>	<b>1</b>	<b>4</b>	<b>5</b>
Cash	<b>15</b>	-	<b>15</b>
Provisions <sup>24</sup>	<b>(3)</b>	-	<b>(3)</b>
Other net assets (liabilities)	<b>(22)</b>	-	<b>(22)</b>
Net identifiable assets (liabilities)	<b>(9)</b>	<b>48</b>	<b>39</b>
Non-controlling interests			<b>(4)</b>
Goodwill			<b>10</b>
Purchase consideration			<b>45</b>

Subsequent to the effective date of the acquisition on January 1, 2009, the RHI Group purchased the remaining shares in Memory held by third parties to give the RHI Group a 100% interest in Memory. The cash consideration was \$5 million, which has been recorded to equity as a change in ownership interest in subsidiaries.

Goodwill represents a control premium and synergies that can be obtained from the RHI Group's existing business. None of the goodwill recognized is expected to be deductible for income tax purposes.

The fair value of other net assets (liabilities) includes receivables with a fair value of \$1 million.

Directly attributable acquisition-related costs of \$1 million were incurred in this acquisition. These are reported within the operating result of the Pharmaceuticals operating segment.

**Memory Acquisition – 2009: net cash outflow** *in millions of USD*

	Cash consideration paid	Cash in acquired company	Net cash outflow
Memory	<b>(45)</b>	<b>15</b>	<b>(30)</b>

The above cash consideration paid does not include the subsequent payment of \$5 million to purchase the remaining shares in Memory held by third parties to give the RHI Group a 100% interest in Memory. This is reported as financing cash flow in the statement of cash flows within the heading 'Change in ownership interest in subsidiaries'.

### Contingent consideration arrangements

The RHI Group is party to certain contingent consideration arrangements arising from business combination arrangements. The provisions for these arrangements are recorded as part of other provisions (see Note 24) and are set out in the table below.

#### Provisions for contingent consideration arrangements in millions of USD

	2010	2009
At January 1	-	-
Additional provisions created	-	-
Unused amounts reversed	-	-
Utilised during the year	-	-
Unwinding of discount	-	-
Business combinations <sup>6</sup>		
- Marcadia	90	-
- Minor business combinations	-	-
At December 31	90	-
Expected outflow of resources		
- Within one year	-	-
- Between one to two years	-	-
- Between two to three years	90	-
- More than three years	-	-
Total provisions	90	-

## 7. Global restructuring plans

### Genentech transaction: restructuring and integration

On July 21, 2008 the Roche Group announced an offer to purchase all outstanding shares of Genentech. Following the closing of a transaction, Genentech's South San Francisco site would become the headquarters of the RHI Group's combined pharmaceuticals operations in the United States. On July 21, 2008 the Roche Group also announced that the Roche's pharmaceuticals business in the U.S. would close manufacturing operations at its site in Nutley, New Jersey, and commercial operations would be moved to Genentech. The research site at Palo Alto, California, would be closed with the research activities being transferred to Nutley and to Genentech. Subsequent to these announcements, initial restructuring activities started at the Nutley and Palo Alto sites in 2008.

As described in Note 3, the Genentech transaction was completed effective March 26, 2009. Following this the Pharmaceuticals Division initiated a detailed integration program to align the Genentech business and the rest of the Roche's pharmaceuticals business. Genentech's South San Francisco site has now been established as the headquarters of the pharmaceuticals business in the U.S., including commercial operations for the U.S. market. Genentech Research and Early Development has been set up as an autonomous unit while Genentech's late-stage development activities have been integrated with the global Pharmaceuticals Division network. The integration program included prioritizing projects within the shared portfolio and eliminating activities that were either duplicated or no longer required, notably in the administration function.

Following the completion of the transaction, the Pharmaceuticals Division carried out a detailed reassessment of its global manufacturing network, with particular emphasis on its biotech manufacturing facilities. As a result several manufacturing facilities and construction projects have been discontinued, notably a bulk drug production unit on part of the site at Vacaville in California.

These restructuring activities have been substantially completed by the end of 2010.

**Genentech transaction: restructuring and integration costs** *in millions of USD*

	2010	2009
Employee-related costs		
- Termination costs	<b>16</b>	179
- Pensions and other post-employment benefits	<b>6</b>	(30)
- Genentech stock options: accelerated vesting expenses <sup>10</sup>	-	209
- Other retention plans and other employee benefits	<b>13</b>	37
- Other employee-related costs	<b>73</b>	88
Total employee-related costs	<b>108</b>	483
Site closure costs		
- Impairment of property, plant and equipment	<b>1</b>	839
- Accelerated depreciation of property, plant and equipment	<b>24</b>	63
- Other site closure costs	<b>56</b>	151
Total site closure costs	<b>81</b>	1,053
Impairment of intangible assets	-	214
Other reorganization expenses	<b>217</b>	100
Total	<b>406</b>	1,850

## Operational Excellence

On November 17, 2010 the Roche Group announced details concerning the 'Operational Excellence' global restructuring plan. The plan is aimed at adapting cost structures to an increasingly challenging market environment and achieving significant efficiency and productivity gains. The planned measures will enable sustained investment in research and product development and thus strengthen the Roche Group's long-term innovation capability.

Implementation plans include reducing the work force by 3,550 positions in the United States over the next two years. The planned job reductions will occur in the Pharmaceuticals Division, particularly division's global sales and marketing organization and in manufacturing. Approximately 800 jobs would be transferred to other Roche sites outside the United States.

As part of its plans, the Roche Group intends to seek buyers for its Pharmaceuticals Division manufacturing sites at Florence, South Carolina and Boulder, Colorado in the United States, which would affect additional 600 jobs, and for the research and development site at Madison, Wisconsin, in the United States. These plans are still at a preliminary stage and all of these sites are still in operation. Following a comprehensive portfolio review, the Pharmaceuticals Division has decided to discontinue certain activities in research and early development. In addition certain product development activities are being discontinued or transferred to other Roche sites or to third parties. As a result of these decisions intangible assets with a carrying value of \$129 million were fully impaired during 2010.

The Roche Group currently anticipates that these restructuring activities will be substantially completed by the end of 2012.

### Operational Excellence: restructuring costs in millions of USD

	2010
Employee-related costs	
- Termination costs	<b>278</b>
- Pensions and other post-employment benefits	<b>(72)</b>
- Other employee-related costs	<b>7</b>
<b>Total employee-related costs</b>	<b>213</b>
Site closure costs	
- Impairment of property, plant and equipment	<b>17</b>
- Accelerated depreciation of property, plant and equipment	-
- Environmental remediation costs	<b>1</b>
- Other site closure costs	<b>31</b>
<b>Total site closure costs</b>	<b>49</b>
Impairment of intangible assets	<b>129</b>
Other reorganization expenses	<b>16</b>
<b>Total</b>	<b>407</b>

### Classification of Operational Excellence restructuring costs in millions of USD

			2010
	Depreciation, amortization and impairment	Other costs	Total
Cost of sales			
- Pharmaceuticals	<b>11</b>	<b>18</b>	<b>29</b>
Marketing and distribution			
- Pharmaceuticals	-	<b>79</b>	<b>79</b>
Research and development			
- Pharmaceuticals	<b>129</b>	<b>147</b>	<b>276</b>
General and administration			
- Pharmaceuticals	<b>5</b>	<b>18</b>	<b>23</b>
<b>Total</b>	<b>145</b>	<b>262</b>	<b>407</b>
Total by operating segment			
- Pharmaceuticals	<b>145</b>	<b>262</b>	<b>407</b>

## 8. Employee benefits

<b>Employee remuneration in millions of USD</b>		
	2010	2009
Wages and salaries	<b>3,247</b>	3,208
Social security costs	<b>202</b>	190
Defined contribution post-employment plans	<b>158</b>	165
Operating expenses for defined benefit post-employment plans <sup>9</sup>	<b>30</b>	68
Equity compensation plans <sup>10</sup>	<b>194</b>	436
Termination costs		
- Genentech transaction: restructuring and integration <sup>7</sup>	<b>16</b>	179
- Operational excellence <sup>7</sup>	<b>278</b>	-
Other employee benefits	<b>268</b>	510
Employees' remuneration included in operating results	<b>4,393</b>	4,756
Expected return on plan assets for defined benefit post-employment plans <sup>9</sup>	<b>(209)</b>	(184)
Interest cost for defined benefit post-employment plans <sup>9</sup>	<b>222</b>	217
Total employees' remuneration	<b>4,406</b>	4,789

Other employee benefits consist mainly of life insurance schemes and certain other insurance schemes providing medical coverage and other long-term and short-term disability benefits. Other employee benefits in 2009 also include \$177 million expenses related to the Genentech Employee Retention Program. The charges for employee benefits in the operating results are included in the relevant expenditure line by function. The expected return on plan assets and interest costs from defined benefit plans are included as part of financial income and financing costs, respectively (see Note 4).

## 9. Pensions and other post-employment benefits

The RHI Group's objective is to provide attractive and competitive post-employment benefits to employees, while at the same time ensuring that the various plans are appropriately financed and managing any potential impacts on RHI's long-term financial position. Most employees are covered by pension plans sponsored by RHI Group companies. The nature of such plans varies according to legal regulations, fiscal requirements and economic conditions of the countries in which the employees are employed. Other post-employment benefits consist mostly of post-retirement healthcare and life insurance schemes. Post-employment benefit plans are classified for IFRS as 'defined contribution plans' if the RHI Group pays fixed contributions into a separate fund or to a third-party financial institution and will have no further legal or constructive obligation to pay further contributions. All other plans are classified as 'defined benefit plans', even if RHI's potential obligation is relatively minor or has a relatively remote possibility of arising. Consequently most of RHI's post-employment benefit plans are classified as 'defined benefit plans' for the purpose of these financial statements.

### Defined contribution plans

Defined contribution plans typically consist of payments by employees and by the RHI Group to funds administered by third parties. Payments by the RHI Group were \$158 million (2009: \$165 million). No assets or liabilities are recognized in RHI's balance sheet in respect of such plans, apart from regular prepayments and accruals of the contributions withheld from employees' wages and salaries and of RHI's contributions.

### Defined benefit plans

RHI's plans are usually established as trusts independent of the RHI Group and are funded by payments from the RHI Group and by employees. In some cases, the plan is unfunded and the RHI Group pays pensions to retired employees directly from its own financial resources.

Current and past service costs are charged to the appropriate income statement heading within the operating results. Pension plan administration and funding is overseen at a Roche Group corporate level, and any settlement gains and losses resulting from changes in funding arrangements are reported as general and administration expenses within the Corporate segment. The expected returns on plan assets and interest costs are charged to financial income and financing costs, respectively. Actuarial gains and losses are recorded directly in equity. The recognition of pension assets is limited to the total of the present value of any future refunds from the plans or reductions in future

contributions to the plans and any cumulative unrecognized past service costs. Adjustments arising from the limit on the recognition of assets for defined benefit plans are recorded directly in equity.

**Defined benefit plans: expenses** *in millions of USD*

	2010			2009		
	Pension plans	Other post-employment benefit plans	Total	Pension plans	Other post-employment benefit plans	Total
Current service cost	<b>76</b>	<b>19</b>	<b>95</b>	82	16	98
Past service cost	<b>11</b>	<b>12</b>	<b>23</b>	5	7	12
(Gain) loss on curtailments	<b>(72)</b>	<b>(16)</b>	<b>(88)</b>	(41)	(1)	(42)
(Gain) loss on settlement	-	-	-	-	-	-
Total operating expenses	<b>15</b>	<b>15</b>	<b>30</b>	46	22	68
Expected return on plan assets	<b>(177)</b>	<b>(32)</b>	<b>(209)</b>	(155)	(29)	(184)
Interest cost	<b>166</b>	<b>56</b>	<b>222</b>	164	53	217
Total financial (income) expense	<b>(11)</b>	<b>24</b>	<b>13</b>	9	24	33
Total expense recognized in income statement	<b>4</b>	<b>39</b>	<b>43</b>	55	46	101

The funding of RHI's various defined benefit plans is overseen at a Roche Group corporate level. Qualified independent actuaries carry out valuations on a regular basis and for major plans annually as at the balance sheet date. For funded plans, which are usually trusts independent of the Roche Group's finances, the net asset/liability recognized on RHI's balance sheet corresponds to the over/under funding of the plan, adjusted for unrecognized past service costs. For unfunded plans, where the RHI Group meets the pension obligations directly from its own financial resources, a liability for the defined benefit obligation is recorded in RHI's balance sheet. Pension assets and liabilities in different defined benefit plans are not offset unless the RHI Group has a legally enforceable right to use the surplus in one plan to settle obligations in the other plan. Amounts recognized in the balance sheet for post-employment benefits are predominantly non-current and are reported in non-current assets and liabilities.

**Defined benefit plans: funding status** *in millions of USD*

	2010			2009		
	Funded plans	Unfunded plans	Total	Funded plans	Unfunded plans	Total
Fair value of plan assets	<b>2,856</b>	-	<b>2,856</b>	2,641	-	2,641
Defined benefit obligation	<b>(3,754)</b>	<b>(418)</b>	<b>(4,172)</b>	(3,590)	(391)	(3,981)
Over (under) funding	<b>(898)</b>	<b>(418)</b>	<b>(1,316)</b>	(949)	(391)	(1,340)
Unrecognized past service costs	-	<b>(17)</b>	<b>(17)</b>	-	-	-
Reimbursement rights	<b>88</b>	<b>23</b>	<b>111</b>	101	15	116
Net recognized asset (liability)	<b>(810)</b>	<b>(412)</b>	<b>(1,222)</b>	(848)	(376)	(1,224)
Reported as						
- Defined benefit plans	-	-	-	-	-	-
- Reimbursement rights	<b>88</b>	<b>23</b>	<b>111</b>	101	15	116
Post-employment benefit assets	<b>88</b>	<b>23</b>	<b>111</b>	101	15	116
Post-employment benefit liabilities	<b>(898)</b>	<b>(435)</b>	<b>(1,333)</b>	(949)	(391)	(1,340)
Net recognized asset (liability)	<b>(810)</b>	<b>(412)</b>	<b>(1,222)</b>	(848)	(376)	(1,224)

Further detailed information on plan assets and the defined benefit obligation is given below.

**Defined benefit plans: fair value of plan assets and reimbursement rights** *in millions of USD*

			2010		2009	
	Fair value of plan assets	Reimbursement rights	Total	Fair value of plan assets	Reimbursement rights	Total
At January 1	<b>2,641</b>	<b>116</b>	<b>2,757</b>	2,259	84	2,343
Expected return on plan assets	<b>202</b>	<b>7</b>	<b>209</b>	178	6	184
Actuarial gains (losses)	<b>190</b>	<b>(8)</b>	<b>182</b>	213	31	244
Employer contributions	-	<b>(2)</b>	<b>(2)</b>	155	(5)	150
Employee contributions	-	-	-	-	-	-
Benefits paid - funded plans	<b>(177)</b>	-	<b>(177)</b>	(164)	-	(164)
Past service cost	-	-	-	-	-	-
Curtailments	-	<b>(2)</b>	<b>(2)</b>	-	-	-
Settlements	-	-	-	-	-	-
At December 31	<b>2,856</b>	<b>111</b>	<b>2,967</b>	2,641	116	2,757
Invested as			2010			2009
- Shares and other equity instruments			<b>1,731</b>			1,724
- Bonds, debentures and other debt instruments			<b>781</b>			688
- Property			<b>225</b>			229
- Other assets			<b>230</b>			116
Total			<b>2,967</b>			2,757

**Defined benefit plans: defined benefit obligation** *in millions of USD*

			2010		2009	
	Pension plans	Other post-employment benefit plans	Total	Pension plans	Other post-employment benefit plans	Total
At January 1	<b>2,958</b>	<b>1,023</b>	<b>3,981</b>	2,749	842	3,591
Current service cost	<b>76</b>	<b>19</b>	<b>95</b>	82	16	98
Interest cost	<b>166</b>	<b>56</b>	<b>222</b>	164	53	217
Employee contributions	-	-	-	-	-	-
Actuarial (gains) losses	<b>228</b>	<b>(66)</b>	<b>162</b>	128	159	287
Benefits paid - funded plans	<b>(131)</b>	<b>(46)</b>	<b>(177)</b>	(121)	(43)	(164)
Benefits paid - unfunded plans	<b>(16)</b>	<b>(11)</b>	<b>(27)</b>	(8)	(10)	(18)
Past service cost	<b>11</b>	<b>(5)</b>	<b>6</b>	5	7	12
Curtailments	<b>(72)</b>	<b>(18)</b>	<b>(90)</b>	(41)	(1)	(42)
Settlements	-	-	-	-	-	-
At December 31	<b>3,220</b>	<b>952</b>	<b>4,172</b>	2,958	1,023	3,981
Of which						
- Funded plans	<b>3,049</b>	<b>705</b>	<b>3,754</b>	2,803	787	3,590
- Unfunded plans	<b>171</b>	<b>247</b>	<b>418</b>	155	236	391

**Actuarial assumptions**

Actuarial assumptions are unbiased and mutually compatible estimates of variables that determine the ultimate cost of providing post-employment benefits. They are set on an annual basis by local management and actuaries and are subject to approval by Roche Group corporate management and the Roche Group's actuaries. Actuarial assumptions consist of demographic assumptions on matters such as mortality and employee turnover, and financial assumptions on matters such as salary and benefit levels, interest rates, return on investments and costs of medical benefits. The Roche Group operates defined benefit plans in many countries and the actuarial assumptions vary based upon local economic and social conditions.

**Demographic assumptions:** The most significant demographic assumptions relate to mortality rates. The Roche Group's actuaries use mortality tables which take into account historic patterns and expected changes, such as further increases in longevity. The mortality table used for the U.S. was RP2000 projected to 2017.

Rates of employee turnover, disability and early retirement are based on historical behavior within RHI Group companies.

**Financial assumptions:** These are based on market expectations for the period over which the obligations are to be settled. The ranges of assumptions used in the actuarial valuations of the most significant plans are shown below.

**Defined benefit plans: financial actuarial assumptions**

	Weighted average	2010	Weighted average	2009
		Range		Range
Discount rates	<b>5.40%</b>	<b>5.40%</b>	5.79%	5.79%
Expected rates of return on plan assets	<b>7.93%</b>	<b>7.50%-8.00%</b>	7.93%	7.50%-8.00%
Expected rates of salary increases	<b>6.20%</b>	<b>3.00%-6.50%</b>	6.21%	4.50%-6.53%
Immediate medical cost trend rate	<b>8.00%</b>	<b>8.00%</b>	8.20%	8.20%
Ultimate medical cost trend rate (in 2029)	<b>4.50%</b>	<b>4.50%</b>	4.50%	4.50%

Discount rates, which are used to calculate the discounted present value of the defined benefit obligation, are determined with reference to market yields on high-quality corporate bonds. The currency and term of the bonds are consistent with the obligation being discounted. The interest cost included in the income statement is calculated by multiplying the discount rate by the defined benefit obligation.

Expected returns on plan assets are based on market expectations of expected returns on the assets in funded plans over the duration of the related obligation. This takes into account the split of the plan assets between equities, bonds, property and other investments. The calculation includes assumptions concerning expected dividend and interest income, realized and unrealized gains on plan assets and taxes and administration costs borne by the plan. These are based on long-term market expectations and the actual performance is continually monitored by Roche Group corporate management. Due to the long-term nature of the obligations, the assumptions used for matters such as returns on investments may not necessarily be consistent with recent historical patterns. The expected return on plan assets included in the income statement is calculated by multiplying the expected rate of return by the fair value of plan assets. The difference between the expected return and the actual return in any twelve-month period is an actuarial gain/loss and is recorded directly to equity. The actual return on plan assets was a gain of \$392 million (2009 gain of \$391 million).

Expected rates of salary increases, which are used to calculate the defined benefit obligation and the current service cost included in the income statement, are based on the latest expectation and historical behavior within RHI Group companies.

Medical cost trend rates are used to calculate the defined benefit obligation and the current service cost included in the income statement of post-employment medical plans. These take into account the benefits set out in the plan terms and expected future changes in medical costs. The effect of one percentage point increase or decrease in the medical cost trend rate is shown below.

**Defined benefit plans: sensitivity of medical cost trend rate in millions of USD**

	+1%	2010	+1%	2009
		-1%		-1%
Current service cost and interest cost	<b>9</b>	<b>(8)</b>	7	(6)
Defined benefit obligation	<b>106</b>	<b>(88)</b>	105	(88)



## Funding summary

A five-year summary of the funding status of RHI's defined benefit plans is shown in the table below.

### Defined benefit plans: summary of funding status *in millions of USD*

	2010	2009	2008	2007	2006
Funded plans					
- Fair value of plan assets	<b>2,856</b>	2,641	2,259	3,107	2,890
- Defined benefit obligation	<b>(3,754)</b>	(3,590)	(3,276)	(3,169)	(3,115)
- Over (under) funding	<b>(898)</b>	(949)	(1,017)	(62)	(225)
Unfunded plans					
- Defined benefit obligation	<b>(418)</b>	(391)	(315)	(348)	(352)
Increase (decrease) in funding status arising from experience adjustments					
- Fair value of plan assets	<b>190</b>	213	(990)	67	201
- Defined benefit obligation	<b>99</b>	7	63	(86)	(84)
Increase (decrease) in funding status arising from changes in actuarial assumptions					
- Fair value of plan assets	-	-	-	-	-
- Defined benefit obligation	<b>(261)</b>	(294)	(9)	158	92

## Cash flows

The RHI Group incurred cash flows from its defined benefit plans as shown in the table below.

### Defined benefit plans: cash flows *in millions of USD*

	2010	2009
Employer contributions, net of reimbursements – funded plans	<b>2</b>	(150)
Benefits paid – unfunded plans	<b>(27)</b>	(18)
Total cash inflow (outflow)	<b>(25)</b>	(168)

Based on the most recent actuarial valuations, the RHI Group expects that employer contributions for funded plans in 2011 will be approximately \$14 million. Benefits paid for unfunded plans are estimated to be approximately \$25 million.

## Amounts recorded in equity

The actuarial gains and losses recognized in the statement of comprehensive income were gains of \$20 million (2009: losses of \$43 million), pre-tax. The total amount at December 31, 2010 was an accumulated loss of \$606 million (2009: accumulated loss of \$626 million).

## 10. Employee stock options and other equity compensation benefits

The Roche Group operates several equity compensation plans, including separate plans at Genentech (prior to the Genentech transaction). Effective January 1, 2005 RHI adopted IFRS 2: 'Share-based Payment'. Amongst other matters, the standard requires that the fair value of all equity compensation plan awards granted to employees be estimated at grant date and recorded as an expense over the vesting period. The expense is charged against the appropriate income statement heading. General and administration costs in 2009 include \$209 million of expenses from accelerated vesting of Genentech equity compensation plans following the Genentech transaction (see Note 7).

**Expenses for equity compensation plans in millions of USD**

	2010	2009
Cost of sales	<b>28</b>	74
Marketing and distribution	<b>53</b>	53
Research and development	<b>70</b>	57
General and administration	<b>43</b>	252
Total operating expenses	<b>194</b>	436
<b>Share option plans</b>		
Genentech Stock Option Plan	-	296
<b>Other equity compensation plans</b>		
Genentech Employee Stock Purchase Program	-	34
Roche Stock-settled Stock Appreciation Rights	<b>133</b>	82
Restricted Stock Unit Plan	<b>68</b>	14
Roche Performance Share Plan	<b>2</b>	2
Roche Stock Appreciation Rights	<b>(9)</b>	8
Total other equity compensation plans	<b>194</b>	140
Total operating expenses	<b>194</b>	436
of which		
- Equity-settled	<b>203</b>	428
- Cash-settled	<b>(9)</b>	8

**Cash inflow (outflow) from equity compensation plans in millions of USD**

	2010	2009
<b>Genentech equity compensation plans</b>		
Genentech Stock Option Plan	-	74
Genentech Employee Stock Purchase Program	-	25
Total cash inflow from Genentech equity compensation plans	-	99
<b>Other equity-settled plans</b>		
Recharges and prepayments to related parties for other equity compensation plans	<b>(188)</b>	(178)
<b>Cash-settled plans</b>		
- reported in statement of cash flows as part of movements in net working capital (accrued liabilities)		
Roche Stock Appreciation Rights	<b>(18)</b>	(15)

In addition to the above cash flows, upon the completion of the Genentech transaction in 2009 the remaining outstanding Genentech employee stock options were fully redeemed for cash. The resulting cash outflow was \$2,412 million, which was reported as a change in ownership interest in subsidiaries (see Note 3).

**Roche Long-Term:** During 2005 the Roche Group implemented a new global long-term incentive program which is available to certain directors, management and employees selected at the discretion of the Roche Group. The program consists of Stock-settled Stock Appreciation Rights (S-SARs). In 2009, following the integration of Genentech, the Group also established a Restricted Stock Units (RSUs) plan. The first awards of this plan were made in September 2009 to employees at Genentech. The S-SARs are issued in accordance with the Roche S-SAR Plan (the Regulations of January 1, 2005 including amendments effective as of January 1, 2007 and the addenda, including the Roche S-SAR Plan's 2009 Addendum United States as of September 1, 2009). The Remuneration Committee determines the number of non-voting equity securities (Genussscheine) that will be available under the plan each year. The above regulations collectively provide that 60 million non-voting equity securities (Genussscheine) will be available for issuance under the Roche S-SAR Plan over a ten-year period. The RSUs are issued in accordance with the Roche Restricted Stock Unit Plan (the Regulations effective September 1, 2009), under which 10 million non-voting equity securities (Genussscheine) will be available for issuance over a ten-year period. Further details of both plans are given in the relevant sections below.

## Share option plans

**Genentech Stock Option Plan:** The Genentech Stock Option Plan was adopted in 1999 and amended thereafter. In April 2004 Genentech's shareholders approved an equity incentive plan. The plans allowed for the granting of various stock options, incentive stock options and stock purchase rights to employees, directors and consultants of Genentech. No incentive stock options and stock purchase rights have been granted under this plan to date. The options granted, were non-tradable equity-settled awards, had a duration of 10 years and vested on a phased basis over four years, subject to continued employment. Upon the completion of the Genentech transaction (see Note 3) the remaining outstanding options were fully redeemed for cash. For accounting purposes the remaining fair value of \$192 million was expensed for the options that were not fully vested at that time.

### **Genentech Stock Option Plan - movement in number of options outstanding**

	Number of options (millions)	2009 Weighted average exercise price (USD)
Outstanding at January 1	77	63.06
Granted	-	-
Forfeited	-	-
Exercised	(1)	52.66
Expired	-	-
Genentech transaction <sup>3</sup>	(76)	63.14
Outstanding at December 31	-	-
- of which exercisable	-	-

## Other equity compensation plans

**Genentech Employee Stock Purchase Program (ESPP):** Genentech had an employee stock purchase program that allowed employees to purchase Genentech's common stock at 85% of the lower of market value at the grant date or purchase date. In 2009 a total of 0.4 million shares of Genentech common stock were purchased resulting in a cash inflow of \$25 million and the cost of the plan was \$34 million, which was reported within the relevant expenditure line by function. Upon the completion of the Genentech transaction (see Note 3) the remaining outstanding awards were fully redeemed for cash. For accounting purposes the remaining fair value of \$17 million was expensed for the awards that were not fully vested at that time.

**Roche Stock-settled Stock Appreciation Rights:** With the introduction of Roche Long-Term in 2005, the Roche Group offers Stock-settled Stock Appreciation Rights (S-SARs) to certain directors, management and employees selected at the discretion of the Roche Group. The S-SARs give employees the right to receive non-voting equity securities (Genussscheine) reflecting the value of any appreciation in the market price of the non-voting equity securities between the grant date and the exercise date. The rights, which are non-tradable equity-settled awards, have a seven-year duration and vest on a phased basis over three years, subject to continued employment.

### Roche S-SARs - movement in number of rights outstanding

	Number of rights (thousands)	2010 Weighted average exercise price (CHF)	Number of rights (thousands)	2009 Weighted average exercise price (CHF)
Outstanding at January 1	17,712	171.80	7,376	191.33
Granted	13,376	150.61	11,223	158.75
Forfeited	(1,983)	181.33	(622)	190.79
Exercised	(669)	142.39	(333)	131.97
Expired	-	-	-	-
Transfer of expatriate employees	(89)	171.51	68	184.25
Outstanding at December 31	28,347	161.83	17,712	171.80
- of which exercisable	7,985	179.46	4,293	187.50

### Roche S-SARs – terms of rights outstanding at December 31, 2010

Year of grant	Number outstanding (thousands)	Rights outstanding		Rights exercisable	
		Weighted average years remaining contractual life	Weighted average exercise price (CHF)	Number exercisable (thousands)	Weighted average exercise price (CHF)
2005	688	1.18	123.82	688	123.82
2006	949	2.17	195.08	949	195.08
2007	1,230	3.17	229.44	1,230	229.44
2008	2,702	4.12	192.95	1,857	193.03
2009	9,600	5.57	159.63	3,207	159.81
2010	13,178	6.68	150.33	54	175.37
Total	28,347	5.62	161.83	7,985	179.46

The weighted average fair value of the rights granted in 2010 was calculated using a binomial model. The resulting weighted average fair value per right is CHF 13.84, giving a total fair value of 185 million Swiss francs which is charged over the vesting period of three years.

**Roche Restricted Stock Unit Plan:** For the first time in September 2009 the Roche Group issued Restricted Stock Units (RSUs) awards to certain directors, management and employees selected at the discretion of the Roche Group. The RSUs, which are non-tradable, represent the right to receive non-voting equity securities (*Genussscheine*) which vest only after a three-year period. The weighted average fair value of the awards granted in 2010 was 123.55 CHF calculated on the basis of the market value of Roche non-voting equity securities at the date of issue, discounted to take into account that the awards would not accrue for any dividends during the vesting period.

### Roche RSUs - movement in number of awards outstanding

	2010 Number of awards (thousands)	2009 Number of awards (thousands)
Outstanding at January 1	1,247	-
Granted	1,350	1,257
Forfeited	(106)	(10)
Transferred to participants	(4)	-
Transfer of expatriate employees	(11)	-
Outstanding at December 31	2,476	1,247
- of which exercisable	4	-

**Roche Performance Share Plan:** The Roche Group offers future non-voting equity security awards (or, at the discretion of the Roche Group Board of Directors, their cash equivalent) to certain directors and key senior managers. The program was established at the beginning of 2002 and currently operates in annual three-year cycles. The terms of the currently outstanding awards are set out in the table below. The amount of non-voting equity securities allocated will depend upon the individual's salary level, the achievement of performance targets linked to the Roche Group's Total Shareholder Return (shares and non-voting equity securities combined) relative to the Roche Group's peers during the three-year period from the date of the grant, and the discretion of the Roche Group Board of Directors. These are non-

tradable equity-settled awards. Each award will result in between zero and two non-voting equity securities, depending upon the achievement of the performance targets.

**Roche Performance Share Plan – terms of outstanding awards at December 31, 2010**

	2008-2010	2009-2011	2010-2012
Number of awards (thousands)	10	15	20
Vesting period	3 years	3 years	3 years
Allocated to recipients in	Feb. 2011	Feb. 2012	Feb. 2013
Fair value per unit (CHF)	201.22	156.06	173.39

The weighted average fair value of the 21,819 awards granted in 2010 was calculated using a Monte Carlo simulation. The input parameters to the model were the covariance matrix between Roche and the other individual companies of the peer group based on a three-year history and a risk-free rate of 0.59%. The valuation also takes into account the defined rank and performance structure which determines the payout of the plan.

**Roche Stock Appreciation Rights:** Some employees of the RHI Group receive Stock Appreciation Rights (SARs) as part of their compensation. The SARs, which are non-tradable cash-settled awards, may be exercised after a vesting period of between one and three years for a cash payment, based upon the amount by which the market price of the Roche Group's American Depositary Receipts (ADRs) at the point of exercise exceeds the strike price (grant price at issuance). Following the implementation of Roche Long-Term (see above), the Roche Group does not plan to award any further cash-settled SARs and no awards have been made since 2004.

**Roche Stock Appreciation Rights in millions of USD**

	2010	2009
Liability at December 31	5	32
Intrinsic value of vested rights at December 31	5	32

**Roche Stock Appreciation Rights - terms of rights outstanding at December 31, 2010**

Year of grant	Number outstanding and exercisable (thousands)	Rights outstanding and exercisable	
		Expiry	Weighted average exercise price (USD)
2004	514	Feb. 03, 2011	26.04
Total	<b>514</b>		<b>26.04</b>

The fair value at December 31, 2010 was calculated using a binomial model. The inputs to the model were the ADR price at December 31, 2010 (\$36.65), the exercise prices given in the above table, and other inputs consistent with those used for the Roche S-SAR awards 2010 given in the table below.

**Issues of rights in 2010:** Issues of rights in 2010, including the methodology used to calculate fair value and the main inputs to the valuation models, are described below.

**Issues of equity compensation plans in 2010**

	Roche S-SAR
Number of rights granted	13,376 thousand
Underlying equity	Roche non-voting equity securities
Currency	Swiss francs
Vesting period	Progressively over 3 years
Contractual life	7 years
Weighted average fair value of rights issued	13.84
Option pricing model used	Binomial
Inputs to option pricing model	
- Share price at grant date	150.61
- Exercise price	150.61
- Expected volatility	24.01%
- Expected dividend yield	7.51%
- Early exercise factor	1.214
- Expected exit rate	7.63%

Volatility for Roche S-SAR was determined primarily by reference to historically observed prices of the underlying equity. Risk-free interest rates are derived from zero coupon swap rates at the grant date taken from Datastream. The early exercise factor describes the ratio between the expected market price at the exercise date and the exercise price at which early exercises can be expected, based on historically observed behavior.

## 11. Property, plant and equipment

### Property, plant and equipment: movements in carrying value of assets *in millions of USD*

	Land	Buildings and land improvements	Machinery and equipment	Construction in progress	Total
<b>At January 1, 2009</b>					
Cost	505	5,054	4,799	974	11,332
Accumulated depreciation and impairment	-	(1,115)	(2,602)	-	(3,717)
Net book value	505	3,939	2,197	974	7,615
<b>Year ended December 31, 2009</b>					
At January 1, 2009	505	3,939	2,197	974	7,615
Additions	-	28	249	521	798
Disposals	-	(13)	(19)	(43)	(75)
Divestment of subsidiary <sup>33</sup>	-	(58)	(117)	(315)	(490)
Transfers	-	479	306	(785)	-
Depreciation charge	-	(267)	(461)	-	(728)
Impairment charge	-	(568)	(289)	(4)	(861)
Other	-	(1)	-	16	15
At December 31, 2009	505	3,539	1,866	364	6,274
Cost	505	5,484	4,939	368	11,296
Accumulated depreciation and impairment	-	(1,945)	(3,073)	(4)	(5,022)
Net book value	505	3,539	1,866	364	6,274
<b>Year ended December 31, 2010</b>					
At January 1, 2010	<b>505</b>	<b>3,539</b>	<b>1,866</b>	<b>364</b>	<b>6,274</b>
Additions	-	<b>7</b>	<b>185</b>	<b>452</b>	<b>644</b>
Disposals	-	-	<b>(25)</b>	-	<b>(25)</b>
Marcadia acquisition <sup>6</sup>	-	-	-	-	-
Other business combinations <sup>6</sup>	-	-	<b>1</b>	-	<b>1</b>
Transfers	-	<b>229</b>	<b>172</b>	<b>(401)</b>	-
Depreciation charge	-	<b>(255)</b>	<b>(378)</b>	-	<b>(633)</b>
Impairment charge	-	<b>15</b>	<b>(49)</b>	<b>(25)</b>	<b>(59)</b>
Other	-	<b>3</b>	-	-	<b>3</b>
At December 31, 2010	<b>505</b>	<b>3,538</b>	<b>1,772</b>	<b>390</b>	<b>6,205</b>
Cost	<b>505</b>	<b>5,620</b>	<b>5,095</b>	<b>417</b>	<b>11,637</b>
Accumulated depreciation and impairment	-	<b>(2,082)</b>	<b>(3,323)</b>	<b>(27)</b>	<b>(5,432)</b>
Net book value	<b>505</b>	<b>3,538</b>	<b>1,772</b>	<b>390</b>	<b>6,205</b>

Impairment charges arise from changes in the estimates of the future cash flows expected to result from the use of the asset and its eventual disposal. Factors such as changes in the planned use of buildings, machinery or equipment, or closure of facilities, the presence or absence of competition and technical obsolescence could result in shortened useful lives or impairment. Impairment charges of \$13 million (2009: \$25 million) are reported as part of 'Cost of sales', impairment charges of \$41 million including impairment reversals of \$15 million (2009: impairment reversals of \$3 million) are reported in 'Research and development' and impairment charges of \$5 million (2009: impairment charges of \$839 million) are reported within 'General and administration'. The major part of the impairment reported in 'General and administration' in 2009 related to the discontinuation of a bulk drug production unit on part of the site at Vacaville in California (see Note 7).

Borrowing costs totaling \$5 million using a rate of 4.79% (2009: \$8 million using a rate of 4.79%) were capitalized as property, plant and equipment.

## Leasing arrangements where the RHI Group is the lessee

**Finance leases:** As at December 31, 2010 Genentech had leasing arrangements which are described below. There was no other capitalized cost of property, plant and equipment under finance leases (2009: none).

**Genentech leasing arrangements:** In December 2004 Genentech entered into a Master Lease Agreement with Slough SSF, LLC, which was subsequently acquired by Health Care Properties ("HCP"), for the development of property adjacent to Genentech's South San Francisco site. The development includes a total of eight buildings, which are subject to separate agreements as contemplated by the Master Lease Agreement. HCP as the developer will construct the building shell for each building and Genentech will finish the interior of each building as laboratory or office space, as applicable. The construction of the first buildings was completed in 2006, at which point the lease term for those buildings was deemed to begin. Construction of the final buildings was completed during 2008. The lease term expires twelve years from the occupation of the final building. Genentech has two five-year renewal options for each building and has an option to purchase the various buildings at different dates between 2016 and 2020. Genentech also has a right of first refusal with respect to each building or the entire development should HCP consider selling part or all of the development.

As at December 31, 2010 the total carrying value of property, plant and equipment from this agreement was \$186 million (2009: \$205 million) and the carrying value of the leasing obligation was \$253 million (2009: \$264 million). Estimates of the total future minimum lease payments anticipated by the entire Master Lease Agreement are shown below.

### Estimated total future minimum lease payments under HCP leases in millions of USD

	Principal	Ground lease	Interest	Total minimum lease payments
Within one year	15	8	16	39
Between one and five years	83	33	51	167
More than five years	149	40	24	213
Total	247	81	91	419

**Operating leases:** RHI Group companies are party to a number of operating leases, mainly for plant and machinery, including motor vehicles, and for certain short-term property rentals. The arrangements do not impose any significant restrictions on the RHI Group. Total operating lease rental expense was \$94 million (2009: \$87 million).

### Operating leases: future minimum lease payments under non-cancellable leases in millions of USD

	2010	2009
Within one year	63	67
Between one and five years	145	155
More than five years	69	91
Total minimum payments	277	313

## Leasing arrangements where the RHI Group is the lessor

**Finance leases:** Certain assets, mainly diagnostics instruments, are leased to third parties through finance lease arrangements. Such assets are reported as receivables at an amount equal to the net investment in the lease. Lease income from finance leases is recognized over the term of the lease based on the effective interest rate method.

### Finance leases: future minimum lease payments under non-cancellable leases in millions of USD

	Gross investment in lease		Present value of future minimum lease payments	
	2010	2009	2010	2009
Within one year	19	17	16	15
Between one and five years	40	35	36	31
More than five years	-	-	-	-
Total	59	52	52	46
Unearned finance income	(6)	(4)	n/a	n/a
Unguaranteed residual value	n/a	n/a	1	2
Net investment in lease	53	48	53	48

The accumulated allowance for uncollectible minimum lease payments was \$2 million (2009: \$2 million). There were no contingent rents recognized in income.



**Operating leases:** Certain assets, mainly some diagnostics instruments, are leased to third parties through operating lease arrangements. Such assets are reported within property, plant and equipment. Lease income from operating leases is recognized over the lease term on a straight-line basis.

**Operating leases: future minimum lease payments under non-cancellable leases** *in millions of USD*

	2010	2009
Within one year	<b>74</b>	68
Between one and five years	<b>148</b>	147
More than five years	-	2
Total minimum payments	<b>222</b>	217

At December 31, 2010, machinery and equipment with an original cost of \$357 million (2009: \$300 million) and a net book value of \$181 million (2009: \$171 million) was being leased to third parties. There was no contingent rent recognized as income.

**Capital commitments**

The RHI Group has non-cancellable capital commitments for the purchase or construction of property, plant and equipment totaling \$113 million (2009: \$140 million).

## 12. Goodwill

**Goodwill: movements in carrying value of assets** *in millions of USD*

	2010	2009
At January 1	<b>5,537</b>	4,096
Memory acquisition <sup>6</sup>	-	10
Marcadia acquisition <sup>6</sup>	<b>152</b>	-
Other business combinations <sup>6</sup>	<b>41</b>	-
IGEN capital contribution <sup>27</sup>	-	1,431
Impairment charge	-	-
At December 31	<b>5,730</b>	5,537
Allocated to the following cash-generating units		
- Pharmaceuticals	<b>1,932</b>	1,780
Total Pharmaceuticals Division	<b>1,932</b>	1,780
Diagnostics Division		
- Diabetes Care	<b>2</b>	2
- Professional Diagnostics	<b>1,465</b>	1,465
- Molecular Diagnostics	-	-
- Applied Science	<b>233</b>	233
- Tissue Diagnostics	<b>796</b>	755
- Strategic goodwill (held at divisional level and not allocated to business areas)	<b>1,302</b>	1,302
Total Diagnostics Division	<b>3,798</b>	3,757

There are no accumulated impairment losses in goodwill.

**Goodwill impairment testing**

**Pharmaceuticals Division:** For the Pharmaceuticals Division, the recoverable amount used in the impairment testing is based on value in use. The cash flow projections used are based on the most recent business plans approved by management. These assume no significant changes in the organization of the division and include management's latest estimates on sales volume and pricing, and production and other operating costs. These reflect past experience and are projected over five years. The cash flow projections used do not extend beyond management's most recent business plans. The discount rate used is based on a rate of 7.31%, which is derived from a capital asset pricing model using data from Swiss capital markets, including Swiss Federal Government twenty-year bonds and the Swiss Market Index. Cost of debt is calculated based on the weighted average effective interest rate of the bonds and notes issued. A weighted average tax rate of 24.98% is used in the calculations. Management believes that any reasonably possible change in any of the key assumptions would not cause the carrying value of goodwill to exceed the recoverable amount.

**Diagnostics Division:** The division's business areas are the cash-generating units used for the testing of goodwill. The goodwill arising from the Corange/Boehringer Mannheim acquisition and part of the goodwill from the Ventana acquisition is recorded and monitored at a divisional level as it relates to the strategic development of the whole division and cannot be meaningfully allocated to the division's business areas. Therefore the cash-generating unit for this goodwill is the entire division. The recoverable amount used in the impairment testing is based on value in use. The cash flow projections used are based on the most recent business plans approved by management. These assume no significant changes in the organization of the division and include management's latest estimates on sales volume and pricing, and production and other operating costs. These reflect past experience and are projected over five years. The estimates for the Tissue Diagnostics business area are projected over ten years, which management believes reflects the long-term nature of this business. The cash flow projections used do not extend beyond management's most recent business plans. The discount rate used is based on a rate of 7.31%, which is derived from a capital asset pricing model using data from Swiss capital markets, including Swiss Federal Government twenty-year bonds and the Swiss Market Index. Cost of debt is calculated based on the weighted average effective interest rate of the bonds and notes issued. A weighted average tax rate of 19.71% is used in the calculations. Management believes that any reasonably possible change in any of the key assumptions would not cause the carrying value of goodwill to exceed the recoverable amount.

## 13. Intangible assets

### **Intangible assets: movements in carrying value of assets** *in millions of USD*

	Product intangibles: in use	Product intangibles: not available for use	Marketing intangibles: in use	Technology intangibles: in use	Total
<b>At January 1, 2009</b>					
Cost	4,534	1,540	-	655	6,729
Accumulated amortization and impairment	(2,822)	(29)	-	(534)	(3,385)
Net book value	1,712	1,511	-	121	3,344
<b>Year ended December 31, 2009</b>					
At January 1, 2009	1,712	1,511	-	121	3,344
Memory acquisition <sup>6</sup>	-	44	-	-	44
IGEN capital contribution <sup>27</sup>	444	-	-	-	444
Additions	6	146	-	12	164
Disposals	-	(73)	-	(50)	(123)
Amortization charge	(286)	-	-	(18)	(304)
Impairment charge	(169)	(267)	-	(27)	(463)
At December 31, 2009	1,707	1,361	-	38	3,106
Cost	4,962	1,644	-	616	7,222
Accumulated amortization and impairment	(3,255)	(283)	-	(578)	(4,116)
Net book value	1,707	1,361	-	38	3,106
Allocation by operating segment					
- Pharmaceuticals	484	841	-	38	1,363
- Diagnostics	1,223	520	-	-	1,743
Total RHI Group	1,707	1,361	-	38	3,106
<b>Year ended December 31, 2010</b>					
At January 1, 2010	<b>1,707</b>	<b>1,361</b>	-	<b>38</b>	<b>3,106</b>
Marcadia acquisition <sup>6</sup>	<b>93</b>	<b>206</b>	-	-	<b>299</b>
Other business combinations <sup>6</sup>	<b>17</b>	<b>51</b>	-	<b>3</b>	<b>71</b>
Additions	<b>31</b>	<b>150</b>	-	-	<b>181</b>
Disposals	<b>(10)</b>	<b>(12)</b>	-	-	<b>(22)</b>
Transfers	<b>16</b>	<b>(16)</b>	-	-	-
Amortization charge	<b>(239)</b>	-	-	<b>(7)</b>	<b>(246)</b>
Impairment charge	<b>(16)</b>	<b>(203)</b>	-	<b>(24)</b>	<b>(243)</b>
At December 31, 2010	<b>1,599</b>	<b>1,537</b>	-	<b>10</b>	<b>3,146</b>
Cost	<b>5,110</b>	<b>2,022</b>	-	<b>620</b>	<b>7,752</b>
Accumulated amortization and impairment	<b>(3,511)</b>	<b>(485)</b>	-	<b>(610)</b>	<b>(4,606)</b>
Net book value	<b>1,599</b>	<b>1,537</b>	-	<b>10</b>	<b>3,146</b>
Allocation by operating segment					
- Pharmaceuticals	<b>549</b>	<b>965</b>	-	<b>6</b>	<b>1,520</b>
- Diagnostics	<b>1,050</b>	<b>572</b>	-	<b>4</b>	<b>1,626</b>
Total RHI Group	<b>1,599</b>	<b>1,537</b>	-	<b>10</b>	<b>3,146</b>

**Significant intangible assets as at December 31, 2010 in millions of USD**

	Operating segment	Net book value	Remaining amortization period
<b>Product intangibles in use</b>			
Tanox acquisition	Pharmaceuticals	376	9 years
Ventana acquisition	Diagnostics	525	7 years
IGEN capital contribution <sup>27</sup>	Diagnostics	272	6 years
<b>Product intangibles not available for use</b>			
Ventana acquisition	Diagnostics	516	n/a

**Classification of amortization and impairment expenses in millions of USD**

	2010		2009	
	Amortization	Impairment	Amortization	Impairment
Cost of sales				
- Pharmaceuticals	<b>62</b>	-	105	-
- Diagnostics	<b>177</b>	<b>16</b>	179	15
Marketing and distribution				
- Diagnostics	-	-	-	-
Research and development				
- Pharmaceuticals	<b>7</b>	<b>227</b>	18	213
- Diagnostics	-	-	2	21
General and administration				
- Pharmaceuticals	-	-	-	214
<b>Total</b>	<b>246</b>	<b>243</b>	304	463

**Internally generated intangible assets**

The RHI Group currently has no internally generated intangible assets from development as the criteria for the recognition as an asset are not met.

**Intangible assets with indefinite useful lives**

The RHI Group currently has no intangible assets with indefinite useful lives.

**Impairment of intangible assets**

Impairment charges arise from changes in the estimates of the future cash flows expected to result from the use of the asset and its eventual disposal. Factors such as the presence or absence of competition, technical obsolescence or lower than anticipated sales for products with capitalized rights could result in shortened useful lives or impairment.

**2010:** In 2010 the Pharmaceuticals operating segment recorded an impairment charge of \$227 million and the Diagnostics operating segment recorded an impairment charge of \$16 million.

Of the amount recorded in the Pharmaceuticals operating segment, an impairment charge of \$129 million was recorded as part of the Operational Excellence program (see Note 7). As part of the program the division carried out a comprehensive portfolio review and decided to discontinue certain activities in research and early development. In addition certain product development activities are being discontinued or transferred to other Roche sites or to third parties. As a result of these decisions intangible assets with a carrying value of \$129 million were fully written down.

Apart from the Operational Excellence program, an impairment charge of \$95 million was also recorded in the Pharmaceuticals Division with respect of product intangibles not available for use and follows from recent clinical data and portfolio prioritization decisions relating to certain projects either with alliance partners or acquired in business combinations. The assets concerned, which were not yet being amortized, were fully written down by these charges. A further charge of \$18 million was recorded, resulting from a portfolio prioritization decision on a project acquired as part of a previous business combination. The asset concerned, which was not yet being amortized, was written down to its recoverable value of \$36 million, based on a value in use calculation using a discount rate of 7.31%. A reversal of previously recorded impairment loss of \$15 million was recorded, which follows from the latest clinical data assessment of the project concerned.

In the Diagnostic operating segment, an impairment charge of \$16 million was recorded. This was in respect of intangible assets in use and followed the regular updating of the division's business plans and technology assessments in the second half of 2010. The assets concerned were written down to their recoverable amount of \$13 million, based on a value in use calculation using a discount rate of 7.31%.

**2009:** In 2009 the Pharmaceuticals operating segment recorded an impairment charge of \$427 million and the Diagnostics operating segment recorded an impairment charge of \$36 million.

In the Pharmaceuticals operating segment an impairment charge of \$214 million was recorded related to the Pharmaceuticals Division reorganization (see Note 7). The integration program included prioritizing projects within the shared portfolio. The assets concerned were fully written down by these charges. An impairment charge of \$207 million was recorded in respect of product intangibles not available for use and followed from recent clinical data and portfolio prioritization decisions relating to certain projects either with alliance partners or acquired from business combinations. The assets concerned, which were not yet being amortized, were written down to their recoverable amount of \$127 million, based on a value in use calculation using a discount rate of 7.7%. In addition an impairment charge of \$6 million was recorded relating to intangible assets in use. These followed the regular updating of the division's business plans and technology assessments in the second half of 2009. The assets were written down to their recoverable amount of \$27 million, based on a value in use calculation using a discount rate of 7.7%.

The Diagnostics operating segment recorded an impairment charge of \$36 million. This was in respect of intangible assets in use and followed the regular updating of the division's business plans and technology assessments in the second half of 2009. The assets were written down to their recoverable amount of \$32 million, based on a value in use calculation using a discount rate of 7.7%.

#### **Potential commitments from alliance collaborations**

The RHI Group is party to in-licensing and similar arrangements with its alliance partners. These arrangements may require the RHI Group to make certain milestone or other similar payments dependent upon the achievement of agreed objectives or performance targets as defined in the collaboration agreements.

RHI's current estimate of future third party commitments for such payments is set out in the table below. These figures are not risk adjusted, meaning that they include all such potential payments that can arise assuming all projects currently in development are successful. The timing is based on RHI's current best estimate.

#### **Potential future third-party collaboration payments as at December 31, 2010 in millions of USD**

	Pharmaceuticals	Diagnostics	RHI Group
Within one year	107	1	108
Between one and two years	33	-	33
Between two and three years	97	-	97
Total	237	1	238

## 14. Associates

The RHI Group has no investments in associates (2009: none).

## 15. Financial and other long-term assets

### **Financial and other long-term assets** *in millions of USD*

	2010	2009	2008
Available-for-sale investments	<b>65</b>	92	331
Held-to-maturity investments	-	4	15
Loans receivable	-	-	3
Long-term trade receivables	<b>1</b>	2	1
Restricted cash	<b>9</b>	-	-
Other	<b>37</b>	32	21
<b>Total financial long-term assets</b>	<b>112</b>	130	371
Long-term employee benefits	<b>236</b>	214	212
Other	<b>92</b>	103	110
<b>Total other long-term assets</b>	<b>328</b>	317	322

Financial long-term assets are held for strategic purposes and are classified as non-current. The available-for-sale investments are mainly equity investments. These are primarily investments in private biotechnology companies, which are kept as part of RHI's strategic alliance efforts. Some unquoted equity investments classified as available-for-sale are measured at cost, as their fair value cannot be measured reliably. The carrying value of equity investments held at cost is \$15 million (2009: \$32 million, 2008: \$24 million). Loans receivable comprise all loans to third parties with a term of over one year.

## 16. Inventories

### **Inventories** *in millions of USD*

	2010	2009	2008
Raw materials and supplies	<b>296</b>	271	240
Work in process	<b>90</b>	135	127
Intermediates	<b>869</b>	838	1,176
Finished goods	<b>680</b>	644	556
Less: provision for slow-moving and obsolete inventory	<b>(256)</b>	(162)	(93)
<b>Total inventories</b>	<b>1,679</b>	1,726	2,006

In 2010 expenses relating to inventories expensed through cost of sales totaled \$3,653 million (2009: \$3,405 million).

## 17. Accounts receivable

### **Accounts receivable** *in millions of USD*

	2010	2009	2008
Trade accounts receivable	<b>1,879</b>	1,927	1,892
Notes receivable	<b>8</b>	7	-
Other	<b>16</b>	15	14
Allowances for doubtful accounts	<b>(30)</b>	(21)	(28)
Charge-backs and other allowances	<b>(141)</b>	(66)	(53)
<b>Total accounts receivable</b>	<b>1,732</b>	1,862	1,825

In 2010 expenses relating to bad debt expensed through marketing and distribution totaled \$9 million (2009: income of \$1 million). Significant concentrations within trade receivables of counterparty credit risk are described in Note 30.

The movements in allowances are shown below.

**Allowances for doubtful accounts receivable: movements in recognized liability** *in millions of USD*

	2010	2009
At January 1	<b>(21)</b>	(28)
Additional allowances created	<b>(9)</b>	(4)
Unused amounts reversed	<b>1</b>	5
Utilized during the year	-	-
Other	<b>(1)</b>	6
At December 31	<b>(30)</b>	(21)

## 18. Other current assets

**Other current assets** *in millions of USD*

	2010	2009	2008
Accrued interest income	-	-	1
Derivative financial instruments <sup>23</sup>	-	29	79
Other	<b>368</b>	324	353
Total financial current assets	<b>368</b>	353	433
Prepaid expenses	<b>140</b>	197	177
Other	<b>26</b>	10	17
Total non-financial current assets	<b>166</b>	207	194
Total other current assets	<b>534</b>	560	627

## 19. Marketable securities

### Marketable securities in millions of USD

	2010	2009	2008
<b>Financial assets at fair-value-through-profit-or-loss</b>			
Held-for-trading investments			
- Bonds and debentures	-	-	971
Total financial assets at fair-value-through-profit-or-loss	-	-	971
<b>Held-to-maturity financial assets</b>			
- Money market instruments and time accounts over three months	4	11	-
Total held-to-maturity financial assets	4	11	-
<b>Available-for-sale financial assets</b>			
- Shares	224	240	33
- Bonds and debentures	-	18	3,732
- Money market instruments and time accounts over three months	-	-	1,646
Total available-for-sale financial assets	224	258	5,411
Total marketable securities	228	269	6,382

Marketable securities are held for fund management purposes and are classified as current. Other investments held for strategic purposes are classified as non-current (see Note 15). During 2009 all held-for-trading investments, which had been held at Genentech, were sold.

**Shares:** These consist primarily of readily saleable equity securities.

**Bonds and debentures:** As at 31 December 2010, the RHI Group did not hold any bonds and debentures. The carrying values and contracted maturity of debt securities are shown below.

### Bonds and debentures in millions of USD

	2010	2009	2008
Contracted maturity			
Within one year	-	-	1,643
Between one and five years	-	-	2,443
More than five years	-	18	617
Total bonds and debentures	-	18	4,703

**Money market instruments:** These are contracted to mature within one year of December 31, 2010.

## 20. Cash and cash equivalents

### Cash and cash equivalents in millions of USD

	2010	2009	2008
Cash			
- Cash in hand and in current or call accounts	-	10	262
Cash equivalents			
- Time accounts with a maturity of three months or less	-	-	2,648
Total cash and cash equivalents	-	10	2,910
Cash overdraft	(88)	-	-
Total cash and cash equivalents in the statement of cash flows	(88)	10	2,910



## 21. Accounts payable

### **Accounts payable** in millions of USD

	2010	2009	2008
Trade accounts payable	<b>436</b>	528	385
Other taxes payable	<b>37</b>	37	76
Other accounts payable	<b>60</b>	57	65
Total accounts payable	<b>533</b>	622	526

## 22. Accrued and other current liabilities

### **Accrued and other current liabilities** in millions of USD

	2010	2009	2008
Deferred income	<b>302</b>	405	67
Accrued payroll and related items	<b>782</b>	924	875
Interest payable	<b>934</b>	1,031	60
Derivative financial instruments <sup>23</sup>	<b>7</b>	-	31
Other accrued liabilities	<b>1,755</b>	2,087	2,099
Cash overdrafts	<b>88</b>	-	-
Total accrued and other current liabilities	<b>3,868</b>	4,447	3,132

## 23. Derivative financial instruments

The RHI Group uses derivative financial instruments as part of its risk management activities. This is discussed in Note 30. Derivative financial instruments are carried at fair value. The methods used for determining fair value are described in Note 1.

### **Derivative financial instruments** in millions of USD

	Assets			Liabilities		
	2010	2009	2008	2010	2009	2008
Foreign currency derivatives						
- Other	-	-	20	-	-	(31)
Interest rate derivatives						
- Swaps	-	10	19	-	-	-
Other derivatives	-	19	40	<b>(7)</b>	-	-
Total derivative financial instruments <sup>18, 22</sup>	-	29	79	<b>(7)</b>	-	(31)

### **Derivative financial instruments related parties** in millions of USD

	Assets			Liabilities		
	2010	2009	2008	2010	2009	2008
Foreign currency derivatives						
- Forward exchange contracts	<b>114</b>	-	-	<b>(45)</b>	(204)	-
- Cross-currency swaps	<b>380</b>	1,637	-	-	-	-
Total derivative financial instruments related parties	<b>494</b>	1,637	-	<b>(45)</b>	(204)	-

Derivative financial assets with related parties are included in 'accounts receivable – related parties'. The decline compared to December 31, 2009 is mainly due to a strengthening of the U.S. dollar compared to the euro and pound sterling during 2010. This was offset by foreign currency transaction gains on the non-U.S. dollar denominated bonds and notes (see Note 26). Derivative financial liabilities with related parties are included in 'accounts payable – related parties'.

### **Hedge accounting**

The RHI Group's accounting policy on hedge accounting, which is described in Note 1, requires that to qualify for hedge accounting the hedging relationship must meet several strict conditions on documentation, probability of occurrence, hedge effectiveness and reliability of measurement.

As described in Note 30, the RHI Group has financial risk management policies for foreign exchange risk, interest rate risk, market risk, credit risk and liquidity risk. When deemed appropriate, certain of the above risks are managed by using derivatives. While many of these transactions can be considered as hedges in economic terms, if the required conditions are not met, then the relationship does not qualify for hedge accounting. In this case the hedging instrument and the hedged item are reported independently as if there were no hedging relationship, which means that any derivatives are reported at fair value, with changes in fair value included in financial income.

The RHI Group generally limits the use of hedge accounting to certain significant transactions. Consequently as at December 31, 2010 the RHI Group has no fair value hedges, cash flow hedges or hedges of net investment in a foreign entity that meet the strict requirements to qualify for hedge accounting, apart from those described below.

### Cash flow hedges

The RHI Group has issued bonds and notes in 2009 to finance the Genentech transaction (see Note 26). On some of the bonds and notes which are denominated in euros and sterling, the RHI Group has entered into cross-currency swaps with related parties to hedge foreign exchange and interest rate risk. These cash flow hedges qualify for hedge accounting. As at December 31, 2010 such instruments, which are designated and qualify for hedge accounting, are recorded as assets with a fair value of \$380 million (2009: assets of \$1,637 million). There was no ineffective portion.

The expected undiscounted cash flows from qualifying cash flow hedges, including interest payments during the duration of the derivative contract and final settlement on maturity, are shown in the table below. The decline in expected cash flows is due to a stronger U.S. dollar against euro and pound sterling.

#### Expected cash flows of qualifying cash flow hedges in millions of USD

	Total	0-3 months	4-6 months	7-12 months	1-2 years	2-3 years	3-4 years	4-5 years	Over 5 years
<b>Year ended December 31, 2010</b>									
Cash inflows	<b>17,993</b>	<b>730</b>	-	-	<b>730</b>	<b>7,704</b>	<b>407</b>	<b>1,333</b>	<b>7,089</b>
Cash outflows	<b>(17,703)</b>	<b>(801)</b>	-	-	<b>(803)</b>	<b>(7,486)</b>	<b>(431)</b>	<b>(1,281)</b>	<b>(6,901)</b>
Total	<b>290</b>	<b>(71)</b>	-	-	<b>(73)</b>	<b>218</b>	<b>(24)</b>	<b>52</b>	<b>188</b>
<b>Year ended December 31, 2009</b>									
Cash inflows	20,159	786	-	-	786	786	8,311	438	9,052
Cash outflows	(18,503)	(801)	-	-	(801)	(803)	(7,485)	(431)	(8,182)
Total	1,656	(15)	-	-	(15)	(17)	826	7	870

The undiscounted cash flows in the table above will affect profit and loss as shown below. These include interest payments during the duration of the derivative contract but do not include the final settlement on maturity. The decline in expected cash flows is due to a stronger US dollar against euro and pound sterling.

#### Expected cash flows of qualifying cash flow hedges with impact on profit and loss in millions of USD

	Total	0-3 months	4-6 months	7-12 months	1-2 years	2-3 years	3-4 years	4-5 years	Over 5 years
<b>Year ended December 31, 2010</b>									
Cash inflows	<b>4,116</b>	<b>730</b>	-	-	<b>730</b>	<b>730</b>	<b>407</b>	<b>407</b>	<b>1,112</b>
Cash outflows	<b>(4,424)</b>	<b>(801)</b>	-	-	<b>(803)</b>	<b>(798)</b>	<b>(431)</b>	<b>(431)</b>	<b>(1,160)</b>
Total	<b>(308)</b>	<b>(71)</b>	-	-	<b>(73)</b>	<b>(68)</b>	<b>(24)</b>	<b>(24)</b>	<b>(48)</b>
<b>Year ended December 31, 2009</b>									
Cash inflows	5,220	786	-	-	786	786	786	438	1,638
Cash outflows	(5,225)	(801)	-	-	(801)	(803)	(798)	(431)	(1,591)
Total	(5)	(15)	-	-	(15)	(17)	(12)	7	47

The changes in the hedging reserve within equity are shown in Note 27.

### Fair value hedges

As at December 31, 2009 the RHI Group had hedged some of its fixed-term debt instruments with interest rate swaps. These instruments, which had been designated and qualified as fair value hedges, were recorded in the balance sheet as at December 31, 2009 as assets with a fair value of \$10 million. These instruments expired in July 2010 when the

underlying bond was repaid. During 2010 a loss of \$10 million was recorded on these interest rate swaps (2009: loss of \$9 million). As the fair value hedge had been highly effective since inception, the result of the interest rate swaps was largely offset by changes in the fair value of the hedged debt instruments.

The RHI Group has equity investments in various biotechnology companies that are subject to a greater risk of market fluctuation than the stock market in general. To manage part of this exposure the RHI Group has entered into forward contracts, which have been designated and qualify as fair value hedges. As at December 31, 2010 such instruments are recorded as liabilities with a fair value of \$7 million (2009: assets \$19 million). During 2010 a loss of \$26 million was recorded on these forward contracts (2009: loss of \$21 million). The result of the forward contracts is offset by the changes in the fair value of the hedged equity investments.

The RHI Group uses other derivatives, not designated in a qualifying hedge relationship, to manage its exposures to foreign currency, interest rate, equity market and credit risks. The instruments used may include interest rate swaps, cross-currency swaps, forwards contracts, options.

## 24. Provisions and contingent liabilities

### Provisions: movements in recognized liabilities *in millions of USD*

	Legal provisions	Environmental provisions	Restructuring provisions	Employee provisions	Other provisions	Total
<b>Year ended December 31, 2009</b>						
At January 1, 2009	126	93	121	142	220	702
Memory acquisition <sup>6</sup>	-	-	2	-	1	3
IGEN capital contribution <sup>27</sup>	-	-	8	-	-	8
Additional provisions created	450	42	308	86	289	1,175
Unused amounts reversed	(79)	(2)	(17)	(11)	(31)	(140)
Utilized during the year	(41)	(6)	(84)	(92)	(163)	(386)
Unwinding of discount <sup>4</sup>	5	12	-	-	-	17
Other	-	-	-	6	-	6
At December 31, 2009	461	139	338	131	316	1,385
Of which						
- Current portion	446	16	317	46	311	1,136
- Non-current portion	15	123	21	85	5	249
Total provisions	461	139	338	131	316	1,385
<b>Year ended December 31, 2010</b>						
At January 1, 2010	461	139	338	131	316	1,385
Business combinations <sup>6</sup>						
- Acquired companies	-	-	-	-	-	-
- Contingent considerations	-	-	-	-	90	90
Additional provisions created	398	37	344	80	244	1,103
Unused amounts reversed	(37)	(13)	(34)	(4)	(17)	(105)
Utilized during the year	(60)	(13)	(226)	(68)	(153)	(520)
Unwinding of discount <sup>4</sup>	5	11	-	-	-	16
Other	-	-	-	(1)	-	(1)
At December 31, 2010	767	161	422	138	480	1,968
Of which						
- Current portion	717	10	418	57	378	1,580
- Non-current portion	50	151	4	81	102	388
Total provisions	767	161	422	138	480	1,968
<b>Expected outflow of resources</b>						
- Within one year	717	10	418	57	378	1,580
- Between one to two years	30	7	3	20	12	72
- Between two to three years	6	6	1	12	90	115
- More than three years	14	138	-	49	-	201
Total provisions	767	161	422	138	480	1,968

### Legal provisions

Legal provisions consist of a number of separate legal matters, including claims arising from trade, in various RHI Group companies. The majority of any cash outflows for these other matters are expected to occur within the next one to three years, although these are dependent on the development of the various litigations. Significant provisions are discounted between 4% and 5% where the time value of money is material.

### Environmental provisions

Provisions for environmental matters include various separate environmental issues. By their nature the amounts and timings of any outflows are difficult to predict. The estimated timings of these cash outflows are shown in the table above. Significant provisions are discounted by between 5% and 6% where the time value of money is material.

### Restructuring provisions

These arise from planned programs that materially change the scope of business undertaken by the RHI Group or the manner in which business is conducted. Such provisions include only the costs necessarily entailed by the restructuring which are not associated with the recurring activities of the RHI Group. The timings of these cash outflows are

reasonably certain and are shown in the table above. These provisions are not discounted as the time value of money is not material in these matters.

### **Employee provisions**

These mostly relate to certain employee benefit obligations, such as sabbatical leave and long-service benefits. The timings of these cash outflows can be reasonably estimated based on past performance and are shown in the table above. These provisions are not discounted as the time value of money is not material in these matters.

### **Other provisions**

Other provisions consist mostly of claims arising from trade, sales returns, certain employee benefit obligations and various other provisions from RHI Group companies that do not fit into the above categories. The timings of cash outflows are by their nature uncertain and the best estimates are shown in the table above. These provisions are not discounted as the time value of money is not material in these matters.

### **Contingent liabilities**

The operations and earnings of the RHI Group continue, from time to time and in varying degrees, to be affected by political, legislative, fiscal and regulatory developments, including those relating to environmental protection. The industries in which the RHI Group operates are also subject to other risks of various kinds. The nature and frequency of these developments and events, not all of which are covered by insurance, as well as their effect on future operations and earnings, are not predictable.

The RHI Group has entered into strategic alliances with various companies in order to gain access to potential new products or to utilize other companies to help develop the RHI Group's own potential new products. Potential future payments may become due to certain collaboration partners achieving certain milestones as defined in the collaboration agreements. RHI's best estimate for future commitment payments are given in Note 13.

### **Pharmaceuticals legal cases**

**Accutane:** Hoffmann-La Roche Inc. ('HLR') and various other Roche affiliates have been named as defendants in numerous legal actions in the United States relating to the acne medication Accutane. The litigation alleges that Accutane caused certain serious conditions, including, but not limited to, inflammatory bowel disease ('IBD'), birth defects and psychiatric disorders. As of December 31, 2010 HLR was defending approximately 2,422 actions brought in various federal and state courts throughout the United States for personal injuries allegedly resulting from their use of Accutane. Most of the actions allege IBD as a result of Accutane use. On June 26, 2009 HLR announced that, following a re-evaluation of its portfolio of medicines that are now available from generic manufacturers, rapidly declining brand sales in the U.S. and high costs from personal-injury lawsuits that it continues to defend vigorously, it had decided to immediately discontinue the manufacture and distribution of the product in the United States.

All of the actions pending in federal court alleging IBD were consolidated for pre-trial proceedings in a Multi-District Litigation in the United States District Court for the Middle District of Florida, Tampa Division. In July 2007 the District Court granted summary judgment in favor of HLR in the lead federal IBD cases. The plaintiffs appealed and in August 2008 these rulings were affirmed by the United States Court of Appeals for the Eleventh Circuit. In October 2009 the District court granted summary judgment in favor of HLR in the next five federal IBD cases. The plaintiffs appealed in November 2009 and in May 2010 these rulings were affirmed by the United States Court of Appeals for the Eleventh Circuit. Several recently filed matters remain pending.

All of the actions pending in state court in New Jersey alleging IBD were consolidated for pre-trial proceedings in the Superior Court of New Jersey, Law Division, Atlantic County. As of December 31, 2010 juries in the Superior Court have ruled in favor of the plaintiff in six cases, assessing total compensatory damages totaling \$48 million. The first verdict was reversed on appeal; the re-trial resulted in a verdict in favor of the plaintiff assessing total compensatory damages of \$25.2 million; HLR is currently in the process of post-trial briefing. The second verdict was reversed on appeal; the re-trial is scheduled for May 2011; additional plaintiffs may be added to the trial. HLR has appealed the third verdict to the Superior Court of New Jersey, Appellate Division, which involved three plaintiffs. The next trial, involving three plaintiffs, is scheduled for February 2011.

In October 2007 a jury in the Circuit Court of Escambia County, Florida, returned a verdict in favor of the plaintiff, assessing total compensatory damages of \$7 million, subsequently reduced to \$6.8 million by the court, against the Company. In October 2009, the District Court of Appeal, State of Florida reversed and entered judgment as to HLR. The Supreme Court of Florida declined to review plaintiff's appeal.

Additional trials may be scheduled for 2011. Individual trial results depend on a variety of factors, including many that are unique to the particular case and therefore the trial results to date may not be predictive of future trial results. The RHI Group continues to defend vigorously the remaining personal injury cases and claims.

**Boniva:** HLR and various other Roche affiliates have been named as defendants in numerous legal actions in the United States relating to the post-menopausal osteoporosis medication Boniva. In these litigations, the plaintiffs allege that Boniva caused one of the following conditions: osteonecrosis of jaw ("ONJ"), atypical femoral fractures, or severe bone pain. As of December 31, 2010 HLR is defending approximately 30 actions brought in federal and state courts in the States of New Jersey, New York and California for personal injuries allegedly resulting from the use of Boniva.

All of these Boniva cases are in the early discovery stages of litigation, with no trial dates having been set. Individual trial results depend on a variety of factors, including many that are unique to the particular case. HLR and the other named Roche affiliates intend to vigorously defend themselves in these matters. The outcome of these matters cannot be determined at this time.

**Cabilly patent:** On May 30, 2008 Centocor, Inc. filed a patent lawsuit against Genentech and City of Hope National Medical Center in the U.S. District Court for the Central District of California. The lawsuit related to U.S. Patent No. 6,331,415 ("the Cabilly patent") that is co-owned by Genentech and City of Hope. The Cabilly patent, which expires in 2018, relates to methods used by Genentech and others to make certain antibodies or antibody fragments, as well as cells and DNA used in these methods. Genentech has licensed the Cabilly patent to other companies and derives significant royalties from these licences. The lawsuit sought a declaratory judgment of patent invalidity and unenforceability with regard to the Cabilly patent and of patent non-infringement with regard to certain of Centocor's products. On August 30, 2010 Genentech and Centocor entered into a settlement agreement resolving this lawsuit and certain additional patent issues. The agreement was effective as of April 30, 2010 with regard to royalties that Centocor has agreed to pay for licenses under the Cabilly patent. This matter has been finally resolved.

On October 8, 2009 Glaxo Group Limited, SmithKline Beecham Corporation, and GlaxoSmithKline LLC (collectively "GSK") filed a patent lawsuit against Genentech and City of Hope in the U.S. District Court for the Southern District of Florida. The lawsuit relates to the Cabilly patent and seeks a declaratory judgment of patent invalidity and unenforceability with regard to the Cabilly patent and of patent non-infringement with regard to a certain GSK product. On December 16, 2009 Genentech filed a motion to dismiss, or in the alternative to transfer to the Central District of California. GSK dismissed its Florida lawsuit in its entirety on February 17, 2010 and filed a related action on the same day in Northern District of California. Genentech filed a motion to transfer to the Central District of California, an answer, and a counterclaim against GSK on March 10, 2010. On April 12, 2010 Genentech's motion to transfer was granted. On October 13, 2010 the Court entered an Order related to claim construction matters, including setting a Markman hearing date of February 14, 2011. The outcome of this matter cannot be determined at this time.

**Other litigation:** On June 28, 2003 Mr Ubaldo Bao Martinez filed a lawsuit against the Porriño Town Council and Genentech España S.L. in the Contentious Administrative Court Number One of Pontevedra, Spain. The lawsuit challenged the Town Council's decision to grant licenses to Genentech España S.L. for the construction and operation of a warehouse and biopharmaceutical manufacturing facility in Porriño, Spain. On January 16, 2008 the Administrative Court ruled in favor of Mr Bao on one of the claims in the lawsuit and ordered the closing and demolition of the facility, subject to certain further legal proceedings. On February 12, 2008, Genentech España S.L. and the Town Council filed appeals of the Administrative Court decision at the High Court in Galicia, Spain. On March 16, 2010 Genentech received notice that it prevailed over Mr Bao on the appeal. This decision revokes the January 2008 ruling in its entirety.

On October 4, 2004 Genentech received a subpoena from the United States Department of Justice, requesting documents related to the promotion of Rituxan. Genentech co-operated with the government's associated investigation. Previously the investigation had been both civil and criminal in nature. Genentech was informed in August 2008 by the criminal prosecutor who handled this matter that the government has declined to prosecute Genentech criminally in connection with this investigation. The civil matter was still ongoing. Through counsel Genentech continued to have discussions with government representatives about the status of their investigation and Genentech's views on this matter, including potential resolution. On October 20, 2009 the government notified Genentech that it had decided not to make any civil claim against Genentech. The government's investigation was initiated by a complaint that was filed under seal in the U.S. District Court for the Eastern District of Pennsylvania in 2003 by an individual plaintiff. The complaint was unsealed on December 31, 2009 and is currently the basis of civil litigation by the plaintiff against Roche Holdings, Inc. and Genentech. Discovery in this matter is ongoing. The Group intends to vigorously defend itself. The outcome of this civil litigation cannot be determined at this time.

HLR, Roche Laboratories Inc. ('RLI') and Genentech, along with approximately 50 other brand and generic pharmaceutical companies, have been named as defendants in several legal actions in the United States relating to the pricing of pharmaceutical drugs and State Medicaid reimbursement. The primary allegation in these litigations is that the pharmaceutical companies misrepresented or otherwise reported inaccurate Average Wholesale Prices ('AWP') and/or Wholesale Acquisition Costs ('WAC') for their drugs, which prices were allegedly relied upon by the States in calculating Medicaid reimbursements to entities such as retail pharmacies. The States, through their respective Attorney General, are seeking repayment of the amounts they claim were over-reimbursed. The time period associated with these cases is 1991-2005. As of December 31, 2010, HLR and RLI are defending six actions filed in the following States: Alabama, Mississippi, New Jersey, Kansas, Oklahoma and Louisiana. Genentech is defending one action filed in the state of Kansas. Discovery is currently pending in each of these cases. HLR, RLI and Genentech intend to vigorously defend themselves in these matters. The outcome of these matters cannot be determined at this time.

HLR, along with various other branded pharmaceutical companies, has been named as a defendant in several legal actions in the United States brought by retail pharmacies relating to the discounting practices for Brand Name Prescription Drugs ('BNPD'). In these BNPD litigations, the plaintiffs allege that they were denied discounts for certain prescription drugs that were offered to other mail order and managed care entities, which denial is claimed to be a violation of the Robinson-Patman Act ('RPA'). The RPA is a Federal law that prohibits unlawful price discrimination. In addition, the plaintiffs alleged that the defendants conspired in their refusal to offer them certain discounts. The conspiracy claims against all defendants were previously settled, with only the RPA claims remaining to be litigated. As of December 31, 2010 HLR is defending approximately 10 BNPD actions brought by approximately 120 retail pharmacies in various federal and state courts throughout the United States. Discovery is currently pending in each of these cases. HLR is not currently scheduled for a trial in any of these BNPD matters in 2011. HLR intends to vigorously defend itself. The outcome of these matters cannot be determined at this time

On November 19, 2007 Novartis Vaccines & Diagnostics, Inc. (the former Chiron affiliate of Novartis) filed a lawsuit against Trimeris, Inc. and four Roche Group companies: Hoffmann-La Roche Inc., F. Hoffmann-La Roche Ltd, Roche Laboratories Inc. and Roche Colorado Corp., in the U.S. District Court for the Eastern District of Texas. The complaint sought an injunction and damages for the manufacture and sale of Roche's anti-AIDS drug Fuzeon in the United States. Novartis alleged that these activities infringed the claims of U.S. Patent No. 7,285,271. On September 23, 2010 the matter was settled by Roche and Trimeris taking a royalty-bearing license under the Novartis patent.

On May 8, June 11, August 8, and September 29, of 2008, Genentech was named as a defendant, along with InterMune, Inc. and its former chief executive officer, W. Scott Harkonen, in four separate class-action complaints filed in the U.S. District Court for the Northern District of California on behalf of plaintiffs who allegedly paid part or all of the purchase price for a product that was licensed by Genentech to Connecticut Corporation and was subsequently assigned to InterMune. Genentech responded to these complaints with a motion to dismiss these matters, which was granted on April 28, 2009. Plaintiffs filed amended complaints including only State law claims on May 28, 2009. Genentech responded to these complaints with another motion to dismiss, which was heard on September 11, 2009. The Court again granted Genentech's motion to dismiss with respect to all claims, but with leave for plaintiffs to replead specific claims under California unfair competition law. Plaintiffs filed an amended class action complaint on December 23, 2009 naming Genentech as a defendant in claims for unfair competition law, false advertising law, consumer remedies law, consumer protection law, and unjust enrichment. Genentech sought dismissal of this amended complaint. On September 1, 2010 the Court entered an order granting Genentech's motion to dismiss all claims against it with prejudice. Plaintiffs filed an appeal of the District Court's ruling with the United States Court of Appeals for the Ninth Circuit and briefing on the appeal is ongoing. The outcome of this matters cannot be determined at this time.

On October 27, 2008 Genentech and Biogen Idec Inc. filed a complaint against Sanofi-Aventis Deutschland GmbH ('Sanofi'), Sanofi-Aventis U.S. LLC and Sanofi-Aventis U.S. Inc. in the Northern District of California seeking a declaratory judgment that certain Genentech products, including Rituxan, do not infringe Sanofi's U.S. Patents 5,849,522 and 6,218,140 and a declaratory judgment that the '522 and '140 patents are invalid. Also on October 27, 2008 Sanofi filed suit against Genentech and Biogen Idec in the Eastern District of Texas, Lufkin Division, claiming that Rituxan and at least eight other Genentech products infringe the '522 and '140 patents. Sanofi brought claims for preliminary and permanent injunctions, compensatory and exemplary damages, and other relief. Genentech challenged the venue of the Texas case and, after an opinion by the Federal Circuit Court of Appeals, the Texas and California cases were consolidated in the Northern District of California. The District Court issued a claim construction order on June 23, 2010. Sanofi filed a motion for reconsideration that was denied. Genentech and Biogen Idec have filed motions for summary judgment that Sanofi has opposed and no ruling on these motions has been issued. Discovery in these consolidated

matters is ongoing. In addition on October 24, 2008 Hoechst GmbH filed with the ICC International Court of Arbitration (Paris) a request for arbitration with Genentech, relating to a terminated agreement between Hoechst's predecessors and Genentech that pertained to the above patents and related patents outside the United States. Hoechst is seeking payments on royalties on sales of Genentech products, damages for breach of contract, and other relief. The ICC arbitration hearing was held on August 30, 2010 through September 3, 2010. Post-hearing briefs have been filed and a ruling is expected in the first half of 2011. The outcome of these matters cannot be determined at this time.

On May 11, 2010 Genentech, filed a patent lawsuit against the University of Pennsylvania in the U.S. District Court for the Northern District of California. The lawsuit relates to United States Patent No. 6,733,752 and seeks a declaratory judgment of patent non-infringement and invalidity with regard to that patent. On July 12, 2010 the University counterclaimed against Genentech for infringement of the '752 patent, seeking unspecified damages based on the sales of Herceptin. Genentech filed its answer on August 2, 2010. A case management conference was held on August 24, 2010 and a Markman hearing is currently scheduled for March 28, 2011. Discovery in this matter is ongoing. The outcome of this matter cannot be determined at this time.

On August 27, 2010 PDL Biopharma filed a complaint against Genentech in Nevada state court seeking a judicial declaration concerning Genentech's obligation to pay royalties on certain ex-U.S. sales of Herceptin, Avastin, Xolair and Lucentis under a 2003 agreement between the parties. On September 13, 2010 PDL filed a first amended complaint asserting additional claims against Genentech, including breach of contract and breach of the implied covenant of good faith and fair dealing. PDL also asserted new claims against Roche and Novartis for intentional interference with contractual relations. In addition to declaratory relief, PDL is seeking monetary damages including liquidated and punitive damages. On November 1, 2010 Genentech and Roche filed a motion to dismiss for failure to state a claim, and Roche filed an additional motion to dismiss for lack of personal jurisdiction. The outcome of this matter cannot be determined at this time.

On September 20, 2010 GSK and Genentech each filed patent lawsuits against one another (and in the case of GSK, also against Roche Holding Ltd.) in U.S. District Courts for the District of Delaware and the Northern District of California respectively. The lawsuits concern GSK's U.S. Patent Nos. RE41,070 and RE41,555. GSK has asserted claims against Genentech and Roche alleging infringement of the '070 and '555 patents by certain "therapeutic antibody products," although the complaint only specifically refers to Herceptin. In its lawsuit Genentech is seeking a judicial declaration of non-infringement by certain Genentech products. In the Delaware action on November 12, 2010 Genentech filed a motion to dismiss for failure to state a claim and a motion to transfer the case to California. Roche filed a motion to dismiss for lack of personal jurisdiction (and joining Genentech's motion in the event its personal jurisdiction motion is denied). All motions are currently pending. In the California action on December 1, 2010 the Court entered an order staying the California action pending resolution by the Delaware Court of Genentech's motion to transfer. The outcome of these matters cannot be determined at this time.

## 25. Other non-current liabilities

### **Other non-current liabilities** *in millions of USD*

	2010	2009	2008
Deferred income	<b>52</b>	70	100
Other long-term liabilities	<b>36</b>	46	51
Total other non-current liabilities	<b>88</b>	116	151



## 26. Debt

### **Debt: movements in carrying value of recognized liabilities in millions of USD**

	2010	2009
At January 1	<b>48,756</b>	11,228
Proceeds from issue of bonds and notes	-	40,304
Redemption and repurchase of bonds and notes	<b>(8,186)</b>	(7,222)
Increase (decrease) in commercial paper	<b>(83)</b>	(240)
Increase (decrease) in amounts due to related parties	<b>5,400</b>	573
Increase (decrease) in other debt	<b>(32)</b>	(91)
Settlement of Genentech's financing obligations with Lonza <sup>33</sup>	-	225
Divestment of subsidiary <sup>33</sup>	-	(284)
(Gains) losses on redemption and repurchase of bonds and notes, net	<b>244</b>	8
Amortization of debt discount <sup>4</sup>	<b>43</b>	41
(Gains) losses on financial liabilities at fair-value-through-profit-or-loss, net <sup>4</sup>	-	(6)
IGEN capital contribution <sup>27</sup>	-	1,425
Foreign exchange (gains) losses, net	<b>(932)</b>	2,783
Other	<b>2</b>	12
<b>At December 31</b>	<b>45,212</b>	48,756
Consisting of		
- Bonds and notes	<b>29,567</b>	38,407
- Commercial paper	<b>177</b>	260
- Amounts due to related parties	<b>15,215</b>	9,815
- Amounts due to banks and other financial institutions	-	10
- Genentech leasing obligations <sup>11</sup>	<b>253</b>	264
<b>Total debt</b>	<b>45,212</b>	48,756
Reported as		
- Long-term debt	<b>37,873</b>	41,412
- Short-term debt	<b>7,339</b>	7,344
<b>Total debt</b>	<b>45,212</b>	48,756

The fair value of the bonds and notes is \$33.1 billion (2009: \$45.4 billion, 2008: \$3 billion) and the fair value of total debt is \$48.8 billion (2009: \$55.7 billion, 2008: \$11.2 billion). This is calculated based on the observable market prices of the debt instruments or the present value of the future cash flows on the instrument, discounted at a market rate of interest for instruments with similar credit status, cash flows and maturity periods.

There are no pledges on RHI's assets in connection with debt.

## Bonds and notes

### Recognized liabilities and effective interest rates of bonds and notes *in millions of USD*

	Effective interest rate		2010	2009	2008
	Underlying instrument	Including hedging			
<b>U.S. dollar-denominated notes – floating rate</b>					
	3 months LIBOR				
Notes due February 25, 2010, principal 3 billion U.S. dollars	+1.13%	n/a	-	2,999	-
Notes due February 25, 2011, principal 931 million U.S. dollars	+2.10%	n/a	<b>931</b>	930	-
<b>U.S. dollar-denominated notes – fixed rate</b>					
4.50% notes due March 1, 2012, principal 2.5 billion U.S. dollars	4.84%	n/a	-	2,486	-
5.00% notes due March 1, 2014, principal 2.75 billion U.S. dollars <sup>a)</sup>	5.31%	n/a	<b>2,835</b>	2,725	-
6.00% notes due March 1, 2019, principal 4.5 billion U.S. dollars	6.37%	n/a	<b>4,422</b>	4,415	-
7.00% notes due March 1, 2039, principal 2.5 billion U.S. dollars	7.43%	n/a	<b>2,412</b>	2,411	-
<b>European Medium Term Note programme – floating rate</b>					
	3 months EURIBOR				
Notes due March 4, 2010, principal 1.5 billion euros	+1.05%	+0.92%	-	2,150	-
<b>European Medium Term Note programme – fixed rate</b>					
4.625% notes due March 4, 2013, principal 5.25 billion euros	4.82%	5.53%	<b>6,947</b>	7,484	-
5.5% notes due March 4, 2015, principal 1.25 billion pounds sterling	5.70%	5.73%	<b>1,914</b>	1,992	-
5.625% notes due March 4, 2016, principal 2.75 billion euros	5.70%	6.37%	<b>3,641</b>	3,927	-
6.5% notes due March 4, 2021, principal 1.75 billion euros	6.66%	6.99%	<b>2,298</b>	2,477	-
<b>Swiss franc bonds</b>					
2.5% bonds due March 23, 2012, principal amount 2.5 billion Swiss francs	2.68%	3.05%	<b>2,667</b>	2,402	-
<b>U.S. dollar bonds</b>					
'Chameleon' 6.75% due July 6, 2009, principal 487 million U.S. dollars	6.77%	n/a	-	-	493
<b>Genentech Senior Notes</b>					
4.40% Senior Notes due July 15, 2010, principal 500 million U.S. dollars	4.53%	n/a	-	509	519
4.75% Senior Notes due July 15, 2015, principal 1 billion U.S. dollars	4.87%	n/a	<b>1,000</b>	1,000	1,000
5.25% Senior Notes due July 15, 2035, principal 500 million U.S. dollars	5.39%	n/a	<b>500</b>	500	500
<b>Total</b>			<b>29,567</b>	38,407	2,512

a) Of the principal amount of 2.75 billion US dollars, notes of \$1.0 billion will be redeemed on March 24, 2011 following the RHI Group's resolution to early redeem these notes (see below).

**Bonds and notes: maturity** *in millions of USD*

	2010	2009	2008
Within one year	<b>2,028</b>	5,658	493
Between one and two years	<b>2,667</b>	930	519
Between two and three years	<b>6,947</b>	4,888	-
Between three and four years	<b>1,738</b>	7,484	-
Between four and five years	<b>2,914</b>	2,725	-
More than five years	<b>13,273</b>	16,722	1,500
Total bonds and notes	<b>29,567</b>	38,407	2,512

**Unamortized discount included in carrying value of bonds and notes** *in millions of USD*

	2010	2009	2008
U.S. dollar notes	<b>83</b>	215	-
Euro notes	<b>64</b>	88	-
Swiss franc bonds	<b>6</b>	9	-
Sterling notes	<b>13</b>	17	-
Total unamortized discount	<b>166</b>	329	-

**Fair Value Option**

In 2005 the RHI Group applied the Fair Value Option on one of its outstanding debt instruments on which RHI had been applying fair value hedge accounting in the past. This debt instrument was the 'Chameleon' U.S. dollar bonds. This instrument was fully redeemed at its due date in 2009. The Fair Value Option treatment is based on the elimination of an accounting mismatch which had been recognized between the hedging swaps (reported at fair value) and the hedged bonds (reported at amortized cost).

**Issuance of new bonds and notes – 2010**

No new bonds or notes were issued in 2010.

**Issuance of new bonds and notes – 2009**

The RHI Group financed the Genentech transaction (see Note 3) by a combination of the RHI Group's own funds, bonds, notes and commercial paper. The RHI Group raised net proceeds of \$40.3 billion through a series of debt offerings, as described below. All newly issued debt is senior, unsecured and has been guaranteed by Roche Holding Ltd., the parent company of the Roche Group.

**U.S. dollar-denominated notes:** On February 25, 2009 the RHI Group completed an offering of U.S. dollar-denominated notes to qualified institutional buyers in the United States under Rule 144A and to persons other than U.S. persons outside the United States under Regulation S of the U.S. Securities Act of 1933. The RHI Group received approximately \$16.3 billion aggregate net proceeds from the issuance and sale of these fixed and floating rate notes. On March 20, 2009 the RHI Group completed a further offering of U.S. dollar-denominated notes under Rule 144A of the U.S. Securities Act of 1933. Roche received approximately \$2.5 billion in aggregate net proceeds from the issuance and sale of these fixed rate notes. The terms and proceeds of the notes were as follows:

**Issuance of U.S. dollar-denominated notes**

	Principal amount	Net proceeds
	USD millions	USD millions
Floating rate notes due 2010	3,000	2,996
Floating rate notes due 2011	1,250	1,248
Fixed rate 1.95% notes due 2009	2,500	2,500
Fixed rate 4.50% notes due 2012	2,500	2,481
Fixed rate 5.00% notes due 2014	2,750	2,720
Fixed rate 6.00% notes due 2019	4,500	4,409
Fixed rate 7.00% notes due 2039	2,500	2,410
Total	19,000	18,764

**European Medium Term Note programme:** On March 4, 2009 the RHI Group issued euro- and sterling-denominated fixed- and floating rate notes. The terms and proceeds of the notes were as follows:

### Issuance of European Medium Term Notes

	Principal amount EUR millions	Principal amount GBP millions	Net proceeds USD millions
Floating rate EUR notes due 2010	1,500	-	1,883
Fixed rate 4.625% EUR notes due 2013	5,250	-	6,551
Fixed rate 5.5% GBP notes due 2015	-	1,250	1,740
Fixed rate 5.625% EUR notes due 2016	2,750	-	3,441
Fixed rate 6.5% EUR notes due 2021	1,750	-	2,170
Total	11,250	1,250	15,785

Subsequent to the debt issuances, the proceeds of all notes were swapped into U.S. dollars by entering into derivative contracts with related parties. The related party derivatives mirror exactly the terms of derivative contracts that a Roche Group affiliate outside the RHI Group has entered with third party financial institutions. As a result, in these financial statements, the notes have economic characteristics equivalent to U.S. dollar-denominated notes.

**Swiss franc-denominated bonds and notes:** On March 23, 2009 the RHI Group completed an offering of Swiss franc-denominated fixed-rate bonds. The terms and proceeds of the bonds were as follows:

### Issuance of Swiss franc-denominated bonds and notes

	Principal amount CHF millions	Net proceeds USD millions
Fixed rate 1.2% bonds due 2009	4,000	3,548
Fixed rate 2.5% bonds due 2012	2,500	2,207
Total	6,500	5,755

Subsequent to the debt issuances, the proceeds of all Swiss franc-denominated bonds were swapped into U.S. dollars by entering into derivative contracts with related parties. The related party derivatives mirror exactly the terms of derivative contracts that a Roche Group affiliate outside the RHI Group has entered with third party financial institutions. As a result, in these financial statements, the bonds have economic characteristics equivalent to U.S. dollar-denominated bonds.

### Cash inflows from issuance of bonds and notes in millions of USD

	2010	2009
U.S. dollar-denominated notes	-	18,764
European Medium Term Note programme euro- and sterling-denominated notes	-	15,785
Swiss franc-denominated bonds	-	5,755
Total cash inflows from issuance of bonds and notes	-	40,304

### Redemption and repurchase of bonds and notes - 2010

**Redemption of U.S. dollar-denominated notes:** On the due date of February 25, 2010 the RHI Group redeemed notes with a principal of \$3 billion at the original issue amount plus accrued original issue discount ("OID"). The effective interest rate of these notes was 3 months LIBOR plus 1.13%. The cash outflow was \$3,000 million and there was no gain or loss recorded on the redemption.

**Redemption of European Medium Term Note programme notes:** On the due date of March 4, 2010 the RHI Group redeemed notes with a principal of 1.5 billion euros at the original issue amount plus accrued original issue discount ("OID"). The effective interest rate of these notes was 3 months EURIBOR plus 1.05% (plus 0.92% including hedging). The cash outflow was \$2,055 million and there was no gain or loss recorded on the redemption.

**Redemption of Genentech Senior Notes:** On the due date of July 15, 2010 the RHI Group redeemed notes with a principal of \$500 million at the original issue amount plus accrued original issue discount ("OID"). The effective interest rate of these bonds was 4.53%. The cash outflow was \$500 million and there was no gain or loss recorded on the redemption.

**Early redemption of U.S. dollar-denominated notes:** On June 29, 2010 the RHI Group resolved to exercise its option to call for redemption the U.S. dollar denominated 4.50% fixed rate notes due March 1, 2012 with a principal of \$2.5 billion. The RHI Group redeemed these notes on September 9, 2010 at an amount equal to the sum of the present

values of the remaining scheduled payments of these notes discounted to the redemption date at the U.S. Treasury rate plus 0.50%, together with accrued and unpaid interest on the principal. The effective interest rate of these notes before the redemption was 4.84%. The cash outflow was \$2,631 million, plus accrued interest. The loss on redemption of \$141 million is recorded within financing costs (see Note 4).

On December 28, 2010 the RHI Group resolved to exercise its option to call for redemption a portion of the U.S. dollar denominated 5.00% fixed rate notes due March 1, 2014. An amount of \$1.0 billion of the total principal amount of \$2.75 billion will be redeemed on March 24, 2011 at an amount equal to the sum of the present values of the remaining scheduled payments of these notes discounted to the redemption date at the U.S. Treasury rate plus 0.50%, together with accrued and unpaid interest on the principal. The U.S. Treasury rate will be determined by an independent investment banker on the third business day preceding the redemption. A cash outflow of approximately \$1,098 million, plus accrued interest, is expected on redemption. The RHI Group has revised the carrying value of these notes to take into account the changes to the amounts and timings of the estimated cash flows. The revised carrying value of these notes at December 31, 2010 is \$1,097 million. The increase in carrying value of \$103 million is recorded within financing costs (see Note 4) as a loss on redemption. The effective interest rate of these notes is 5.31%.

### Redemption and repurchase of bonds and notes - 2009

**Redemption of 'Chameleon' U.S. dollar bonds:** The RHI Group redeemed these bonds with a remaining outstanding principal value of \$487 million, which had a due date of July 6, 2009, at the original issue amount plus accrued original issue discount ('OID'). The effective interest rate of these bonds was 6.77%. The cash outflow was \$488 million. There was no gain or loss recorded in the income statement upon the redemption.

**Redemption and repurchase of U.S. dollar-denominated notes:** The RHI Group redeemed notes with a principal value of \$2,500 million, which had a due date of September 23, 2009, at the original issue amount plus accrued original issue discount ('OID'). The effective interest rate of these bonds was 1.98%. The cash outflow was \$2,500 million. There was no gain or loss recorded in the income statement upon the redemption.

In addition the RHI Group repurchased floating rate notes with a principal value of \$319 million and original due date of February 25, 2011, at various dates during 2009 in open market purchases. The effective interest rate of these bonds was 3 months LIBOR plus 2.10%. The cash outflow was \$327 million. A loss of \$8 million was recorded in the income statement upon the repurchase.

**Redemption of Swiss franc-denominated notes:** The RHI Group redeemed notes with a principal value of 4,000 million Swiss francs, which had a due date of September 23, 2009, at the original issue amount plus accrued original issue discount ('OID'). The effective interest rate of these bonds was 1.30%, or 2.20% including associated hedging instruments. The cash outflow was \$3,907 million. There was no gain or loss recorded in the income statement upon the redemption.

### Cash outflows from redemption and repurchase of bonds and notes *in millions of USD*

	2010	2009
U.S. dollar-denominated notes	(5,631)	(2,827)
European Medium Term Note program euro-denominated notes	(2,055)	-
Genentech Senior Notes	(500)	-
'Chameleon' U.S. dollar bonds	-	(488)
Swiss franc-denominated notes	-	(3,907)
Total cash outflows from redemption and repurchase of bonds and notes	(8,186)	(7,222)

### Commercial paper

**Genentech commercial paper program:** In October 2007 Genentech established a commercial paper program under which it could issue up to \$1 billion of unsecured commercial paper notes. As at December 31, 2008 unsecured commercial paper notes with a principal amount of \$500 million were outstanding. During the first six months of 2009 the Group fully redeemed these notes at maturity at their principal value. Genentech has terminated its commercial paper program as of May 15, 2009 and there were no amounts outstanding at December 31, 2010.

**Roche Holdings, Inc. commercial paper program:** In March 2009 Roche Holdings, Inc. established a commercial paper program under which it can issue up to \$7.5 billion of unsecured commercial paper notes guaranteed by Roche Holding Ltd. Committed credit lines of 2.5 billion euro and \$950 million are available as back-stop lines. Maturity of the notes under the program cannot exceed 365 days from the date of issuance. At December 31, 2010 unsecured

commercial paper notes with a principal of \$177 million and an interest rate of 0.19% were outstanding. These amounts were due at various dates until January 7, 2011.

**Movements in commercial paper obligations** *in millions of USD*

	2010	2009
At January 1	<b>260</b>	500
Net cash proceeds (payments)		
- Genentech commercial paper program	-	(500)
- Roche Holdings, Inc. commercial paper program	<b>(83)</b>	260
Total net cash proceeds (payments)	<b>(83)</b>	(240)
At December 31	<b>177</b>	260

## Recognized liabilities due to related parties

The movements of the amounts due to related parties are shown in the table below:

### Recognized liabilities due to related parties in millions of USD

		2010	2009	2008
At January 1		<b>9,815</b>	7,817	4,664
Cash inflows from related parties		<b>11,165</b>	963	4,427
Cash outflows to related parties		<b>(5,765)</b>	(390)	(1,274)
IGEN capital contribution <sup>27</sup>		-	1,425	-
At December 31		<b>15,215</b>	9,815	7,817

  

	Effective interest rate	2010	2009	2008
Term note 5.95% due June 7, 2010, principal \$280 million	6.04%	-	280	280
Term note 5.95% due October 15, 2010, principal \$500 million	6.04%	-	500	500
Term note 6.15% due December 16, 2011, principal \$1.5 billion	6.25%	<b>1,500</b>	1,500	1,500
Term note 6.20% due September 17, 2012, principal \$200 million	6.30%	<b>200</b>	250	250
Term note 6.20% due September 17, 2012, principal \$250 million	6.29%	<b>250</b>	250	360
Term note 6.45% due July 17, 2014, principal \$200 million	6.56%	<b>200</b>	500	500
Term note 5.80% due February 12, 2018, principal \$1,4 billion	5.88%	<b>1,400</b>	1,400	1,400
Term note 5.80% due February 12, 2018, principal \$2,0 billion	5.88%	<b>2,000</b>	2,000	2,000
Term note 4.50% due September 19, 2011, principal \$800 million	4.55%	<b>800</b>	800	800
Term note 1.75% due January 19, 2009, principal \$150 million	1.75%	-	-	150
Term note 2.10% due May 5, 2009, principal \$55 million	2.11%	-	-	55
Term note 2.25% due March 15, 2010, principal \$22 million	2.26%	-	22	22
Term note 2.25% due March 15, 2010, principal \$78 million	2.26%	-	78	-
Term note 2.25% due March 15, 2010, principal \$10 million	2.26%	-	10	-
Term note 5.52% due March 14, 2014, principal \$800 million	5.60%	<b>800</b>	800	-
Term note 6.3% due June 25, 2010, principal \$525 million <sup>27</sup>	6.40%	-	525	-
Term note 5.70% due November 13, 2012, principal \$900 million <sup>27</sup>	5.78%	<b>900</b>	900	-
Term note 5.79% due February 25, 2020 principal \$1,500 million	5.88%	<b>1,500</b>	-	-
Term note 0.83% due March 15, 2011, principal \$20 million	0.83%	<b>20</b>	-	-
Term note 0.83% due March 15, 2011, principal \$45 million	0.83%	<b>45</b>	-	-
Term note 5.60% due June 8, 2020, principal \$280 million	5.68%	<b>280</b>	-	-
Term note 0.96% due June 24, 2011, principal \$420 million	0.96%	<b>420</b>	-	-
Term note 2.53% due September 3, 2014, principal \$300 million	2.55%	<b>300</b>	-	-
Term note 0.60% due March 9, 2011, principal \$1,750 million	0.60%	<b>1,750</b>	-	-
Term note 2.25% due March 14, 2014, principal \$500 million	2.26%	<b>500</b>	-	-
Term note 0.59% due March 3, 2011, principal \$600 million	0.59%	<b>600</b>	-	-
Term note 1.99% due January 6, 2014, principal \$1,750 million	2.00%	<b>1,750</b>	-	-
Total amounts due to related parties		<b>15,215</b>	9,815	7,817

**Issues from related parties:** Issues of new term notes from related parties are shown in the table below:

**Cash inflows from related parties** *in millions of USD*

	2010	2009
Term note 2.25% issued March 16, 2009	-	78
Term note 2.25% issued March 16, 2009	-	10
Term note 5.52% issued March 16, 2009	-	800
Term note 0.85% issued June 29, 2009	-	75
Term note 0.94% issued February 25, 2010	<b>500</b>	-
Term note 5.79% issued February 25, 2010	<b>1,500</b>	-
Term note 0.83% issued March 04, 2010	<b>1,000</b>	-
Term note 0.83% issued March 15, 2010	<b>100</b>	-
Term note 0.83% issued March 15, 2010	<b>20</b>	-
Term note 0.83% issued March 15, 2010	<b>45</b>	-
Term note 0.87% issued April 29, 2010	<b>500</b>	-
Term note 5.60% issued June 7, 2010	<b>280</b>	-
Term note 0.96% issued June 25, 2010	<b>420</b>	-
Term note 2.53% issued September 03, 2010	<b>300</b>	-
Term note 0.60% issued September 09, 2010	<b>1,750</b>	-
Term note 0.53% issued October 06, 2010	<b>1,750</b>	-
Term note 2.25% issued October 15, 2010	<b>500</b>	-
Term note 0.46% issued November 02, 2010	<b>150</b>	-
Term note 0.59% issued December 03, 2010	<b>600</b>	-
Term note 1.99% issued December 06, 2010	<b>1,750</b>	-
Total cash inflows from related party issues	<b>11,165</b>	963

**Payments to related parties:** Payments of term notes to related parties are shown in the table below:

**Cash outflows to related party issues** *in millions of USD*

	2010	2009
Term note 6.20% due September 17, 2012, principal \$360 million	-	110
Term note 1.75% due January 19, 2009, principal \$150 million	-	150
Term note 2.10% due May 5, 2009, principal \$55 million	-	55
Term note 0.85% due September 29, 2009, principal \$75 million	-	75
Term note 2.25% due March 15, 2010, principal \$22 million	<b>22</b>	-
Term note 2.25% due March 15, 2010, principal \$10 million	<b>10</b>	-
Term note 2.25% due March 15, 2010, principal \$78 million	<b>78</b>	-
Term note 5.95% due June 7, 2010, principal \$280 million	<b>280</b>	-
Term note 6.40% due June 25, 2010, principal \$525 million	<b>525</b>	-
Term note 0.94% due September 15, 2010, principal \$500 million	<b>500</b>	-
Term note 0.87% due October 6, 2010, principal \$500 million	<b>500</b>	-
Term note 0.83% due October 15, 2010, principal \$100 million	<b>100</b>	-
Term note 5.95% due October 15, 2010, principal \$500 million	<b>500</b>	-
Term note 6.20% due September 17, 2012, principal \$50 million	<b>50</b>	-
Term note 0.83% due December 3, 2010, principal \$1,000 million	<b>1,000</b>	-
Term note 0.46% due December 3, 2010, principal \$150 million	<b>150</b>	-
Term note 0.53% due December 6, 2010, principal \$1,750 million	<b>1,750</b>	-
Term note 6.45% due July 17, 2014, principal \$300 million	<b>300</b>	-
Total cash outflows to related party issues	<b>5,765</b>	390



## 27. Equity attributable to RHI shareholder

### Changes in equity attributable to RHI shareholder in millions of USD

	Share capital	Retained earnings	Fair value reserve	Hedging reserve	Total
<b>Year ended December 31, 2009</b>					
At January 1, 2009	1	7,127	65	7	7,200
Net income recognized in income statement	-	816	-	-	816
Available-for-sale investments					
- Valuation gains (losses) taken to equity	-	-	30	-	30
- Transferred to income statement on sale or impairment	-	-	4	-	4
- Income taxes	-	-	(9)	-	(9)
- Non-controlling interests	-	-	(2)	-	(2)
Cash flow hedges					
- Gains (losses) taken to equity	-	-	-	1,924	1,924
- Transferred to income statement <sup>a)</sup>	-	-	-	(1,817)	(1,817)
- Transferred to the initial carrying value of hedged items	-	-	-	-	-
- Income taxes	-	-	-	(38)	(38)
- Non-controlling interests	-	-	-	(13)	(13)
Defined benefit post-employment plans					
- Actuarial gains (losses) <sup>9</sup>	-	(43)	-	-	(43)
- Income taxes	-	38	-	-	38
- Non-controlling interests	-	-	-	-	-
Other comprehensive income, net of tax	-	(5)	23	56	74
<b>Total comprehensive income</b>	-	<b>811</b>	<b>23</b>	<b>56</b>	<b>890</b>
Capital contribution related parties <sup>27</sup>	-	382	-	-	382
Dividends paid	-	-	-	-	-
Equity compensation plans	-	297	-	-	297
Changes in ownership interests in subsidiaries					
- Genentech <sup>3</sup>	-	(39,050)	-	-	(39,050)
- Memory <sup>6</sup>	-	(1)	-	-	(1)
Changes in non-controlling interests	-	(15)	-	-	(15)
At December 31, 2009	1	(30,449)	88	63	(30,297)

a) Of amounts transferred to income statement losses of \$11 million (2008: losses of \$80 million) were reported as 'Royalties and other operating income' and gains of \$1,828 million (2008: gains of \$3 million) as 'Financial income'.

**Changes in equity attributable to RHI shareholder** *in millions of USD*

	Share capital	Retained earnings	Fair value reserve	Hedging reserve	Total
<b>Year ended December 31, 2010</b>					
At January 1, 2010	<b>1</b>	<b>(30,449)</b>	<b>88</b>	<b>63</b>	<b>(30,297)</b>
Net income recognized in income statement	-	<b>2,104</b>	-	-	<b>2,104</b>
Available-for-sale investments					
- Valuation gains (losses) taken to equity	-	-	<b>90</b>	-	<b>90</b>
- Transferred to income statement on sale or impairment	-	-	<b>(98)</b>	-	<b>(98)</b>
- Income taxes	-	-	<b>4</b>	-	<b>4</b>
Cash flow hedges					
- Gains (losses) taken to equity	-	-	-	<b>(1,316)</b>	<b>(1,316)</b>
- Transferred to income statement <sup>a)</sup>	-	-	-	<b>1,029</b>	<b>1,029</b>
- Transferred to the initial carrying value of hedged items	-	-	-	-	-
- Income taxes	-	-	-	<b>103</b>	<b>103</b>
Defined benefit post-employment plans					
- Actuarial gains (losses) <sup>9</sup>	-	<b>20</b>	-	-	<b>20</b>
- Income taxes	-	<b>(7)</b>	-	-	<b>(7)</b>
Other comprehensive income, net of tax	-	<b>13</b>	<b>(4)</b>	<b>(184)</b>	<b>(175)</b>
Total comprehensive income	-	<b>2,117</b>	<b>(4)</b>	<b>(184)</b>	<b>1,929</b>
Dividends paid	-	-	-	-	-
Equity compensation plans	-	<b>222</b>	-	-	<b>222</b>
Other movements	-	<b>(75)</b>	<b>53</b>	<b>22</b>	-
At December 31, 2010	<b>1</b>	<b>(28,185)</b>	<b>137</b>	<b>(99)</b>	<b>(28,146)</b>

a) Of amounts transferred to income statement gains of \$28 million (2009: losses of \$11 million) were reported as 'Royalties and other operating income' and losses of \$1,057 million (2009: gains of \$1,828 million) as 'Financial income'

The RHI Group completed the purchase of the non-controlling interests in Genentech effective March 26, 2009 (see Note 3). Based on the revised International Accounting Standard 27 'Consolidated and Separate Financial Statements' (IAS 27), which was adopted by RHI in 2008, this transaction was accounted for in full as an equity transaction. As a consequence, the carrying amount of the consolidated equity of the RHI Group was reduced by approximately \$47 billion, of which \$7.6 billion was allocated to eliminate the book value of Genentech non-controlling interests and at December 31, 2010 the RHI Group had a negative equity of \$28.1 billion (December 31, 2009: \$30.3 billion). The capacity of the RHI Group to generate positive cash flows and operating profit is not affected by this accounting treatment.

### Share capital

As of December 31, 2010 the authorized and issued share capital of Roche Holdings, Inc., which is the RHI Group's parent company, consisted of 1,000 shares with a nominal value of \$1,000 each, as in the preceding year. All the shares are indirectly owned by Roche Holding Ltd, a public company registered in Switzerland.

### Own equity instruments

The RHI Group holds none of its own equity shares.

### Reserves

**Fair value reserve:** The fair value reserve represents the cumulative net change in the fair value of available-for-sale financial assets until the asset is sold, impaired or otherwise disposed.

**Hedging reserve:** The hedging reserve represents the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

### Capital contributions related parties - 2009

**IGEN:** On January 1, 2009 the shareholder of Roche Holdings, Inc. contributed the Roche Group's investment in IGEN International, Inc. to RHI as a capital contribution. As a result, RHI obtained a 100% controlling interest in IGEN International, Inc. and its subsidiary BioVeris Corporation effective January 1, 2009. The contributed goodwill was \$1,431

million, intangible assets \$444 million, recognized liabilities due to related parties \$1,425 million and other net liabilities of \$158 million. Their combined recognized net assets at January 1, 2009 were \$384 million, which were reported as an addition of retained earnings in equity. These two companies are reported as part of the Diagnostics operating segment.

**Innovatis Inc:** Effective July 1, 2009, Innovatis AG, a subsidiary of the Roche Group, sold to RHI their 100% ownership of Innovatis Inc, at a nominal prize. Innovatis Inc. was subsequently merged into Roche Diagnostics Corporation, which is part of the Diagnostics operating segment. The fair value of the net liabilities was \$2 million, which was shown as a reduction of equity.

## 28. Non-controlling interests

### **Changes in equity attributable to non-controlling interests** *in millions of USD*

	2010	2009
At January 1	-	6,991
Net income recognized in income statement		
- Genentech <sup>3</sup>	-	375
Total net income recognized in income and expense	-	375
Available-for-sale investments	-	2
Cash flow hedges	-	13
Other comprehensive income, net of tax	-	15
Total comprehensive income	-	390
Memory acquisition <sup>6</sup>	-	4
Equity compensation plans	-	154
Changes in ownership interests in subsidiaries		
- Genentech	-	(7,550)
- Memory <sup>6</sup>	-	(4)
Changes in non-controlling interests	-	15
At December 31	-	-

## 29. Statement of cash flows

### Cash flows from operating activities

Cash flows from operating activities arise from the RHI Group's primary activities in the Pharmaceuticals and Diagnostics businesses. These are calculated by the indirect method by adjusting RHI's operating profit for any operating income and expenses that are not cash flows (for example depreciation, amortization and impairment) in order to derive the cash generated from operations. This and other operating cash flows are shown in the statement of cash flows. Operating cash flows also include income taxes paid on all activities.

#### Cash generated from operations *in millions of USD*

	2010	2009
Net income	<b>2,104</b>	1,191
Add back non-operating (income) expense		
- Financial income <sup>4</sup>	<b>(261)</b>	724
- Financial income – related parties <sup>31</sup>	<b>(55)</b>	(979)
- Financing costs <sup>4</sup>	<b>2,098</b>	1,884
- Financing costs – related parties <sup>31</sup>	<b>992</b>	848
- Income taxes <sup>5</sup>	<b>1,258</b>	179
Operating profit	<b>6,136</b>	3,847
Depreciation of property, plant and equipment <sup>11</sup>	<b>633</b>	728
Amortization of intangible assets <sup>13</sup>	<b>246</b>	304
Impairment of intangible assets <sup>13</sup>	<b>243</b>	463
Impairment of property, plant and equipment <sup>11</sup>	<b>59</b>	861
Operating expenses for defined benefit post-employment plans <sup>9</sup>	<b>30</b>	68
Operating expenses for equity-settled equity compensation plans <sup>10</sup>	<b>203</b>	428
Net (income) expense for provisions <sup>24</sup>	<b>998</b>	1,035
Bad debt expense	<b>9</b>	(1)
Inventory write-downs	<b>226</b>	27
Other adjustments	<b>(2)</b>	19
Cash generated from operations	<b>8,781</b>	7,779

### Cash flows from investing activities

Cash flows from investing activities are principally those arising from the RHI Group's investments in property, plant and equipment and intangible assets, and from the acquisition and divestments of subsidiaries. Cash flows connected with the RHI Group's portfolio of marketable securities and other investments are also included, as are any interest and dividend payments received in respect of these securities and investments. These cash flows indicate the RHI Group's net reinvestment in its operating assets and the cash flow effects of business combinations and divestments, as well as the cash generated by the RHI Group's other investments.

### Cash flows from financing activities

Cash flows from financing activities are primarily the proceeds from the issue and repayment of the RHI Group's equity and debt instruments. They also include interest payments and dividend payments on these instruments. Cash flows from short-term financing, including finance leases, are also included. These cash flows indicate the RHI Group's transactions with the providers of its equity and debt financing. Cash flows from short-term borrowings are shown as a net movement, as these consist of a large number of transactions with short maturity.

### Significant non-cash transactions

**2010:** There were no significant non-cash transactions.

**2009:** In connection with the sale of the subsidiary Genentech Bermuda Ltd., together with its fully-controlled subsidiary, Genentech Singapore, Pte. Ltd. there was a non-cash decrease of \$284 million for the financing obligation for the Singapore Lonza facility and a similar non-cash decrease in the capitalized construction in progress. For further information see Note 33.

## 30. Risk management

### **RHI Group risk management**

Risk management is a fundamental element of the Roche Group business practice on all levels and encompasses different types of risks. At a Roche Group level risk management is an integral part of the business planning and controlling processes. Material risks are monitored and regularly discussed with the Corporate Executive Committee and the Audit Committee of the Board of Directors of Roche Holding Ltd.

### **Financial risk management**

The RHI Group is exposed to various financial risks arising from its underlying operations and corporate finance activities. The RHI Group's financial risk exposures are predominantly related to changes in interest rates, equity prices and to an extent, foreign exchange rates, as well as the creditworthiness and the solvency of RHI's counterparties.

Financial risk management within the Roche Group is governed by policies reviewed by the boards of directors of Roche Holding Ltd. as appropriate to their areas of statutory responsibility. These policies cover credit risk, liquidity risk and market risk. The policies provide guidance on risk limits, type of authorized financial instruments and monitoring procedures. As a general principle, the policies prohibit the use of derivative financial instruments for speculative trading purposes. Policy implementation and day-to-day risk management are carried out by the relevant treasury functions; and regular reporting on these risks is performed by the relevant accounting and controlling functions within Roche Group.

**Carrying value and fair value of financial assets in millions of USD**

By line Items in Notes	Carrying value by asset class					
	Available-for-sale	FVtPL <sup>a)</sup> -held for trading	Held to maturity	Loans and receivables	Total	Fair value
<b>Year ended</b>						
<b>December 31, 2010</b>						
Accounts receivable – third and related parties <sup>b)</sup>	-	494	-	6,010	6,504	6,504
Marketable securities:						
- Money market instruments and time accounts over 3 months	-	-	4	-	4	4
- Shares	224	-	-	-	224	224
Cash and cash equivalents	-	-	-	-	-	-
Derivative financial instruments	-	-	-	-	-	-
Available-for-sale investments	65	-	-	-	65	65
Loans receivable – related parties	-	-	-	89	89	89
Long-term trade receivables	-	-	-	1	1	1
Other financial current assets	-	-	-	368	368	368
Restricted cash	-	-	-	9	9	9
Other long-term assets – third and related parties	-	-	-	375	375	375
<b>Total</b>	<b>289</b>	<b>494</b>	<b>4</b>	<b>6,852</b>	<b>7,639</b>	<b>7,639</b>

By line Items in Notes	Carrying value by asset class					
	Available-for-sale	FVtPL <sup>a)</sup> -held for trading	Held to maturity	Loans and receivables	Total	Fair value
<b>Year ended</b>						
<b>December 31, 2009</b>						
Accounts receivable – third and related parties <sup>b)</sup>	-	1,637	-	6,813	8,450	8,450
Marketable securities:						
- Money market instruments and time accounts over 3 months	-	-	11	-	11	11
- Bonds and debentures	18	-	-	-	18	18
- Shares	240	-	-	-	240	240
Cash and cash equivalents	-	-	-	10	10	10
Derivative financial instruments	-	29	-	-	29	29
Available-for-sale investments	92	-	-	-	92	92
Held-to-maturity investments	-	-	4	-	4	4
Loans receivable – related parties	-	-	-	95	95	95
Long-term trade receivables	-	-	-	2	2	2
Other financial current assets	-	-	-	324	324	324
Other long-term assets – third and related parties	-	-	-	201	201	201
<b>Total</b>	<b>350</b>	<b>1,666</b>	<b>15</b>	<b>7,445</b>	<b>9,476</b>	<b>9,476</b>

a) Fair-value-through-profit-or-loss

b) Derivative financial assets with related parties are included in 'accounts receivable – related parties'

Following the implementation of amendments to IFRS 7 'Financial Instruments: Disclosures' that were published in March 2009 the RHI Group has established a fair value hierarchy that reflects the significance of inputs used in making the fair value measurements. The fair value hierarchy includes the following three levels:

- Level 1 – quoted prices in active markets for identical assets and liabilities
- Level 2 – observable inputs other than quoted prices in active markets for identical assets and liabilities
- Level 3 – unobservable inputs

**Fair value hierarchy of financial assets and liabilities at December 31, 2010 in millions of USD**

	Level 1	Level 2	Level 3	Total
<b>Financial assets recognized at fair value</b>				
Marketable securities:				
- Bonds and debentures	-	-	-	-
- Shares	224	-	-	224
Derivative financial instruments – third and related parties	-	494	-	494
Available-for-sale investments	13	37	-	50
<b>Total</b>	<b>237</b>	<b>531</b>	<b>-</b>	<b>768</b>
<b>Financial liabilities recognized at fair value</b>				
Derivative financial instruments – third and related parties	-	(52)	-	(52)
<b>Total</b>	<b>-</b>	<b>(52)</b>	<b>-</b>	<b>(52)</b>

**Fair value hierarchy of financial assets and liabilities at December 31, 2009 in millions of USD**

	Level 1	Level 2	Level 3	Total
<b>Financial assets recognized at fair value</b>				
Marketable securities:				
- Bonds and debentures	-	-	18	18
- Shares	240	-	-	240
Derivative financial instruments – third and related parties	-	1,666	-	1,666
Available-for-sale investments	48	12	-	60
<b>Total</b>	<b>288</b>	<b>1,678</b>	<b>18</b>	<b>1,984</b>
<b>Financial liabilities recognized at fair value</b>				
Derivative financial instruments – third and related parties	-	(204)	-	(204)
<b>Total</b>	<b>-</b>	<b>(204)</b>	<b>-</b>	<b>(204)</b>

Available-for-sale investments exclude equity securities held at cost of \$15 million (2009: \$32 million), as those are not carried at fair value (see Note 15).

As at December 31, 2010 Level 1 financial assets consist mainly of quoted shares. Level 2 financial assets consist primarily of derivative financial instruments and unquoted shares. At December 31, 2009 Level 3 financial assets consisted of auction-rate student loan securities. These securities were valued based on broker-provided valuation models, which approximate fair value and were sold at par value during 2010. There were no significant transfers between Level 1 and Level 2 and vice versa.

**Changes in fair value of Level 3 financial assets in millions of USD**

	2010	2009
At January 1	18	145
Impairment charges	-	-
Valuation gains (losses) taken to equity	2	24
Gains (losses) recognized in the income statement	-	(42)
Sales	(20)	(109)
<b>At December 31</b>	<b>-</b>	<b>18</b>

**Credit risk**

Credit risk arises from the possibility that counterparties to transactions may default on their obligations, causing financial losses for the RHI Group. The objective of managing counterparty credit risk is to prevent losses of liquid funds deposited with or invested in such counterparties.

The maximum exposure to credit risk resulting from financial activities, without considering netting agreements and without taking account of any collateral held or other credit enhancements, is equal to the carrying value of RHI's financial assets.

**Trade receivables:** These are subject to a policy of active credit risk management which focuses on the assessment of credit availability, ongoing credit evaluation and account monitoring procedures. The objective of the management of trade receivables from third parties is to sustain the growth and profitability of the RHI Group by optimizing asset utilization whilst maintaining risks at an acceptable level. Except as noted below, there is no significant concentration of counterparty credit risk due to the RHI Group's large number of customers. Risk limits and exposures are continuously monitored. Additionally, the RHI Group obtains credit insurance and similar enhancements when appropriate to protect the collection of trade receivables. As at December 31, 2010 no collateral was held for loans and receivables at the end of 2010 (2009: none).

At December 31, 2010 the RHI Group's combined trade accounts receivable balance with three national wholesale distributors, AmerisourceBergen Corp., Cardinal Health Inc. and McKesson Corp., was \$1,217 million representing 65% of RHI's consolidated third party trade accounts receivables (2009: \$1,299 million representing 70%).

**Nature and geographical location of trade receivables (not overdue) counterparties** *in millions of USD*

	2010				2009			
	Total	Public	Wholesale- sellers/dis- tributors	Private	Total	Public	Wholesale- sellers/dis- tributors	Private
Switzerland	1	-	1	-	-	-	-	-
European Union	-	-	-	-	1	-	1	-
Rest of Europe	1	-	-	1	-	-	-	-
North America	1,680	9	1,399	272	1,816	10	1,160	646
Japan	49	-	49	-	50	-	50	-
Rest of Asia	-	-	-	-	-	-	-	-
<b>Total</b>	<b>1,731</b>	<b>9</b>	<b>1,449</b>	<b>273</b>	<b>1,867</b>	<b>10</b>	<b>1,211</b>	<b>646</b>

In addition to third party trade receivable, the RHI Group had \$4.7 billion accounts receivable balances with related parties mainly in the European Union and Switzerland (2009: \$6.6 billion).

**Analysis of overdue but not impaired financial assets by class** *in millions of USD*

	Total amount overdue	Under 1 month	1-3 months	4-6 months	6-12 months	more than 1 year
<b>Year ended December 31, 2010</b>						
Loans and receivables	38	9	18	10	1	-
<b>Year ended December 31, 2009</b>						
Loans and receivables	29	17	4	6	2	-

As at December 31, 2010 there were no financial assets whose terms have been renegotiated (2009: none).

**Liquidity risk**

Liquidity risk arises through a surplus of financial obligations over available financial assets due at any point in time. RHI's approach to liquidity risk is to maintain sufficient readily available reserves in order to meet its liquidity requirements at any point in time.

Roche enjoys strong credit quality and is rated by at least one major credit rating agency. The ratings will permit efficient access to the international capital markets in the event of major financing requirements. In addition, the RHI Group has unused committed credit lines with various financial institutions totaling \$4.3 billion (2009: \$4.5 billion).



**Contractual maturity analysis of financial liabilities** *in millions of USD*

	Total	0-3 months	4-6 months	7-12 months	1-2 years	2-3 years	3-4 years	4-5 years	Over 5 years
<b>Year ended</b>									
<b>December 31, 2010</b>									
Total debt <sup>a)</sup>	<b>61,346</b>	<b>5,861</b>	<b>556</b>	<b>2,912</b>	<b>5,918</b>	<b>8,722</b>	<b>6,710</b>	<b>4,256</b>	<b>26,411</b>
Trade payables	<b>437</b>	<b>435</b>	-	<b>2</b>	-	-	-	-	-
Accruals	<b>2,617</b>	<b>1,868</b>	<b>586</b>	<b>125</b>	<b>38</b>	-	-	-	-
Derivative financial instruments related parties	<b>52</b>	<b>45</b>	-	<b>7</b>	-	-	-	-	-
Other liabilities: current and non-current	<b>131</b>	<b>64</b>	<b>29</b>	-	<b>34</b>	<b>3</b>	-	-	<b>1</b>
<b>Total financial liabilities</b>	<b>64,583</b>	<b>8,273</b>	<b>1,171</b>	<b>3,046</b>	<b>5,990</b>	<b>8,725</b>	<b>6,710</b>	<b>4,256</b>	<b>26,412</b>
<b>Year ended</b>									
<b>December 31, 2009</b>									
Total debt <sup>a)</sup>	67,312	6,971	990	1,696	5,440	8,325	9,340	5,447	29,103
Trade payables	528	527	1	-	-	-	-	-	-
Accruals	2,979	2,677	130	155	17	-	-	-	-
Derivative financial instruments related parties	204	204	-	-	-	-	-	-	-
Other liabilities: current and non-current	140	58	28	1	49	1	1	1	1
<b>Total financial liabilities</b>	<b>71,163</b>	<b>10,437</b>	<b>1,149</b>	<b>1,852</b>	<b>5,506</b>	<b>8,326</b>	<b>9,341</b>	<b>5,448</b>	<b>29,104</b>

a) Total debt in the above table shows undiscounted cash flows, whereas the carrying value in the consolidated balance sheet reflects discounted cash flows.

**Market risk**

Market risk arises from changing market prices of RHI's financial assets or financial liabilities. Market risk may affect RHI's financial result and the value of RHI's equity.

Roche uses Value-at-Risk (VaR) to measure the impact of market risk on its financial instruments. Roche has defined VaR limits to manage market risk. VaR data are reported on a monthly basis and indicate the value range within which a given financial instrument will fluctuate with a pre-set probability as a result of movements in market prices. VaR is a statistical measure which implicitly assumes that value changes of the recent past are indicative of value changes in the future. VaR figures do not represent actual or expected losses, or possible worst-case losses over the stated period. Also, VaR does not consider any effects of favorable market movements.

VaR figures are calculated using a historical simulation approach. For each scenario, all financial instruments are fully valued and the total change in value and earnings is determined. All VaR calculations are based on a 95% confidence level and a holding period of 20 trading days over the past ten years. This holding period reflects the time required to change the corresponding risk exposure, should this be deemed appropriate. Longer holding periods increase the probability of higher value changes and lead to increased VaR figures.

Actual future gains and losses associated with our treasury activities may differ materially from the VaR analyses performed due to the inherent limitations associated with predicting the timing and amount of changes to interest rates, foreign currency exchanges rates and equity investment prices, particularly in periods of high market volatilities. Furthermore, the VaR numbers below do not include the effect of changes in credit spreads.

**Market risk of financial instruments** *in millions of USD*

	December 31, 2010	December 31, 2009
VaR - Foreign exchange component	<b>14</b>	16
VaR - Interest rate component	<b>654</b>	801
VaR - Other price component	<b>24</b>	32
Diversification	<b>(33)</b>	(40)
<b>VaR - Total market risk</b>	<b>659</b>	809

At December 31, 2010, the total VaR of the financial assets and liabilities was \$659 million (2009: \$809 million). The interest rate VaR decreased to \$654 million reflecting the ageing of debt and the repayment of debt during 2010. As all issued debt is held at amortized cost, the interest rate VaR is a sole metric for economic fair value changes, but there is no impact on the carrying value or profit and loss of the Group. The foreign exchange VaR remained stable. Other price risk arises mainly from movements in the prices of equity securities and declined as equity securities holdings were reduced. At December 31, 2010, the RHI Group held equity securities with a market value of \$0.3 billion (December 31, 2009: \$0.3 billion). This includes holdings in biotechnology companies, which were acquired in the context of licensing transactions or scientific collaborations.

### Foreign exchange risk

The RHI Group is exposed to movements in foreign currencies affecting its financial result and the value of RHI's equity. Foreign exchange risk arises because the amount of local currency paid or received for transactions denominated in foreign currencies may vary due to changes in exchange rates (transaction exposures).

The objective of RHI's foreign exchange risk management activities is to preserve the economic value of its current and future assets and to minimize the volatility of RHI's financial result. The primary focus of RHI's foreign exchange risk management activities is on hedging transaction exposures arising through foreign currency flows or monetary positions held in foreign currencies. The RHI Group does not currently hedge translation exposures using financial instruments.

RHI monitors transaction exposures on a daily basis. The net foreign exchange result and the corresponding VaR parameters are reported on a monthly basis. RHI uses forward contracts, foreign exchange options and cross-currency swaps to hedge transaction exposures. Application of these instruments intends to continuously lock in favorable developments of foreign exchange rates, thereby reducing the exposure to potential future movements in such rates.

### Interest rate risk

Interest rate risk arises from movements in interest rates which could affect RHI's financial result or the value of RHI's equity. Changes in interest rates may cause variations in interest income and expense. In addition, they may affect the market value of certain financial assets, liabilities and hedging instruments. The primary objective of RHI's interest rate management is to protect the net interest result.

Interest rate exposures and the corresponding VaR parameters are reported on a monthly basis. RHI uses forward contracts, options and swaps to hedge its interest rate exposures. Depending on the interest rate environment of the major currencies, RHI will use these instruments to generate the appropriate mix of fixed and floating rate exposures.

### Other price risk

Other price risk arises mainly from movements in the prices of equity securities held by RHI. In 2010, the RHI Group held equity securities with a market value of \$0.3 billion (2009: \$0.3 billion). This amount includes holdings in biotechnology companies, which were acquired in the context of licensing transactions or scientific collaborations. Due to the nature of their business, biotechnology companies are exposed to greater equity volatilities than general stock market fluctuations.

RHI manages the price risk through placing limits on individual and total equity investments. These limits are defined both as a percentage of total liquid funds and as an absolute number for individual equity investments.

### Impairment of financial assets

In 2010 impairments of investments were \$2 million (2009: \$4 million).

#### Impairment losses by asset classes *in millions of USD*

	2010	2009
Loans and receivables	(9)	1
Available-for-sale financial assets		
- Shares	-	-
- Investments	(2)	(4)
Total impairment losses	(11)	(3)

## Capital

The RHI Group defines the capital that it manages as RHI's total capitalization, being the sum of debt plus equity, including non-controlling interests. RHI's objectives when managing capital are:

- To safeguard RHI's ability to continue as a going concern, so that it can continue to provide benefits for patients and returns to investors.
- To provide an adequate return to investors based on the level of risk undertaken.
- To have available the necessary financial resources to allow the RHI Group to invest in areas that may deliver future benefits for patients and returns to investors.
- To maintain sufficient financial resources to mitigate against risks and unforeseen events.

Effective March 26, 2009, the purchase of the non-controlling interests in Genentech was completed (see Note 3). Based on the revised International Accounting Standard 27 'Consolidated and Separate Financial Statements' (IAS 27), which was adopted by RHI in 2008, this transaction was accounted for in full as an equity transaction. As a consequence, the carrying amount of the consolidated equity of the RHI Group was reduced by approximately \$47 billion, of which \$7.6 billion was allocated to eliminate the book value of Genentech non-controlling interests. At December 31, 2010 the negative equity of the RHI Group was reduced from \$30.3 billion to \$28.1. The capacity of the RHI Group to generate positive cash flows and operating profit is not affected by this accounting treatment.

Capital is monitored on the basis of the capitalization, which is calculated as being debt plus equity (including non-controlling interests). This is reported to senior management as part of the RHI Group's regular internal management reporting. RHI's capitalization is shown in the table below.

### Capital in millions of USD

	2010	2009	2008
Capital and reserves attributable to RHI shareholder <sup>27</sup>	<b>(28,146)</b>	(30,297)	7,200
Equity attributable to non-controlling interests <sup>28</sup>	-	-	6,991
Total equity	<b>(28,146)</b>	(30,297)	14,191
Total debt <sup>26</sup>	<b>45,212</b>	48,756	11,228
Capitalization	<b>17,066</b>	18,459	25,419

The RHI Group is not subject to regulatory capital adequacy requirements as known in the financial services industry.

## 31. Related parties

### Controlling shareholders

Roche Finance Ltd (Roche Finanz AG), a Swiss corporation, owns all of the issued and outstanding shares of Roche Holdings, Inc. Roche Finance Ltd is a wholly owned, direct subsidiary of Roche Holding Ltd, a public company in Switzerland.

As a member of the Roche Group, all of the RHI Group's related party transactions are with Roche Group affiliates. The transactions include purchases of inventory and other materials, sales of inventory and other materials, allocation of research and development costs under cost-sharing agreements and collaborations, allocation of marketing and distribution costs under cost-sharing agreements, allocations of other expenses attributable to the U.S. business, and the payment and receipt of royalties.

**Related party transactions** *in millions of USD*

	Year ended December 31,	
	2010	2009
Sales	<b>1,273</b>	1,110
Royalty income	<b>1,980</b>	1,806
Contract revenue	<b>132</b>	247
Purchases of inventory and other materials	<b>(461)</b>	(714)
Reimbursements received under marketing and distribution cost sharing agreements	<b>287</b>	2
Reimbursements received under research and development cost sharing and collaboration agreements	<b>822</b>	662
Payments issued under research and development cost sharing and collaboration agreements	<b>(390)</b>	(395)
Profit-sharing expense	-	(6)
Other revenue (expense), net	<b>(43)</b>	(16)
<b>Financial income – related parties</b>		
Gains (losses) on foreign currency derivatives, net	<b>46</b>	942
Other financial income	<b>9</b>	37
Total	<b>55</b>	979
<b>Financing costs – related parties</b>		
Interest expense	<b>(747)</b>	(586)
Guarantee fees	<b>(245)</b>	(258)
Other financial expense	-	(4)
Total	<b>(992)</b>	(848)

A net gain of \$46 million was made on foreign exchange forward contracts with related parties that were entered into to hedge some of the foreign currency transaction exposure arising from bonds and notes issued in euro and Swiss francs. The related party derivatives mirror exactly the terms of derivative contracts that a Roche Group affiliate outside the RHI Group has entered with third party financial institutions. No hedge accounting was applied on those foreign exchange forward contracts. The foreign exchange revaluation losses on the hedged bonds and notes are included in financial income (see Note 4).

**Related party balances** *in millions of USD*

	December 31,		
	2010	2009	2008
Accounts and loans receivable	<b>5,199</b>	6,852	2,085
Accounts and loans payable	<b>(16,293)</b>	(11,036)	(8,564)

The RHI Group deposits surplus funds with Roche Pharmholding B.V. in its function as corporate cash pool leader for numerous Roche affiliates. Amounts deposited of \$3.3 billion are immediately available and bear variable interest referenced to one month LIBOR. In May 2009, after the completion of the purchase of the non-controlling interest of Genentech, Genentech also became a member of this cash pool.

**Subsidiaries and associates**

A listing of the major RHI Group subsidiaries is included in Note 33. Transactions between the parent company and its subsidiaries and between subsidiaries are eliminated on consolidation. The RHI Group has no associates.

## Key management personnel

The purpose of Roche Holdings, Inc. is to act as a holding and financing company for the U.S. operations of the RHI Group and to engage in any lawful act or activity for which a corporation may be organized under the General Corporation Law of Delaware. RHI has no operating functions except through its subsidiaries and the members of the RHI Group Board of Directors act as the chief operating decision-maker.

### Board of Directors of Roche Holdings, Inc.

		Date of appointment
Dr Franz B. Humer	Chairman	May 15, 2001
Dr Erich Hunziker	Vice-Chairman	September 1, 2001
Dr Severin Schwan	Member of the Board	April 29, 2008
Frank J. D'Angelo	Member of the Board	December 2, 2008
Frederick C. Kentz III	Member of the Board	December 2, 2008
David P. McDede	Member of the Board	December 2, 2008
Bruce Resnick	Member of the Board	December 2, 2008

Dr Humer, Dr Hunziker and Dr Schwan did not receive remuneration or payment for their time and expenses related to their services from RHI during 2010 and 2009.

The RHI Group pays to the directors appointed on December 2, 2008 salary, bonus, expense allowance, social insurance contributions in respect of the below remuneration and pays contributions to pension and other post-employment benefit plans. These directors also participate in the equity compensation plans 'Roche Long-Term' and 'Roche Performance Share Plan'. The terms, vesting conditions and fair value of these awards are disclosed in Note 10.

### Remuneration of members of the RHI Group Executive Committee

*in thousands of USD*

	2010	2009
Salaries, including bonuses and expenses	<b>3,417</b>	1,928
Social security costs	<b>75</b>	79
Pensions and other post-employment benefits	<b>215</b>	135
Equity compensation plans	<b>1,159</b>	1,150
Other employee benefits	<b>180</b>	222
Total	<b>5,046</b>	3,514

### Post-employment benefit plans

Transactions between the Group and the various post-employment defined benefit plans for the employees of the RHI Group are described in Note 9.

## 32. Subsequent events

There have been no subsequent events after December 31, 2010.

## 33. Subsidiaries and associates

### Subsidiaries - 2010

Effective January 1, 2010, the Company's wholly-owned subsidiary, Roche Finance USA Inc., was merged into the Company, with the Company being the surviving entity. All the assets and liabilities of Roche Finance USA Inc. were assumed by the Company.

### Subsidiaries - 2009

Effective May 25, 2009, Genentech, Inc. sold Genentech Bermuda Ltd., together with its fully-controlled subsidiary, Genentech Singapore, Pte. Ltd., to F. Hoffmann-La Roche AG, Basel, a subsidiary of Roche Holding Ltd for \$35 million in cash. As a result of the sale these entities were no longer part of the RHI Group. A loss of \$4 million was recognized from this disposal and is included in 'other financial expense' in the related party transactions reported in Note 31. The net cash inflow from the sale was \$27 million. This transaction included the 2006 supply agreement between Genentech, Inc. and Lonza Group Ltd. (Lonza) for the manufacture of certain Genentech products at a facility under construction in Singapore by Lonza. It also included an option to purchase the Lonza Singapore facility. For accounting purposes, due

to the nature of the supply agreement and Genentech's involvement in the construction of the buildings, Genentech, Inc. was considered to be the owner of the assets during the construction period. The sale of the subsidiary Genentech Bermuda Ltd., together with its fully-controlled subsidiary, Genentech Singapore, Pte. Ltd. included construction in progress and the related finance lease obligation. The exclusive purchase option in the original agreement was also transferred.

**Gain (loss) on divestment of subsidiaries - 2009** *in millions of USD*

Consideration received	35
Net assets disposed	
- Property, plant and equipment <sup>11</sup>	(490)
- Cash	(8)
- Finance lease obligation <sup>26</sup>	284
- Other net assets	175
Gain (loss) on divestment	(4)

Subsidiaries and associates	Country of Incorporation	Equity interest %	
		2010	2009
454 Life Sciences Corporation	United States	100%	100%
BioVeris Corporation	United States	100%	100%
Disetronic Medical Systems Inc.	United States	100%	100%
Disetronic Sterile Products	United States	100%	100%
Genentech, Inc.	United States	100%	100%
HLR Consumer Health Inc.	United States	100%	100%
Hoffmann-La Roche Inc.	United States	100%	100%
IGEN International, Inc.	United States	100%	100%
Marcadia Biotech, Inc.	United States	100%	-
Memory Pharmaceuticals Corp.	United States	100%	100%
Roche Carolina, Inc.	United States	100%	100%
Roche Colorado Corporation	United States	100%	100%
Roche Diagnostics Corporation	United States	100%	100%
Roche Diagnostics Operations, Inc.	United States	100%	100%
Roche Finance USA, Inc. <sup>a)</sup>	United States	-	100%
Roche Madison, Inc.	United States	100%	100%
Roche Molecular Systems, Inc.	United States	100%	100%
Roche NimbleGen, Inc.	United States	100%	100%
Roche Palo Alto LLC	United States	100%	100%
Roche Vitamins, Inc.	United States	100%	100%
Spring Bioscience Corp.	United States	100%	100%
Therapeutics Human Polyclonals, Inc.	United States	100%	100%
Ventana Medical Systems, Inc.	United States	100%	100%

a) merged into the Company in 2010

# Report of the RHI Group Auditors

## **Independent Auditor's Report to the Board of Directors of Roche Holdings, Inc., Wilmington, Delaware**

We have audited the accompanying consolidated financial statements of Roche Holdings, Inc., which comprise the income statement, statement of comprehensive income, balance sheet, statement of cash flows, statement of changes in equity and notes on pages 6 to 85 for the year ended December 31, 2010.

**Board of Director's Responsibility:** The Board of Directors is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards (IFRS). This responsibility includes designing, implementing and maintaining an internal control system relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error. The Board of Directors is further responsible for selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

**Auditor's Responsibility:** Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers the internal control system relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control system. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

**Opinion:** In our opinion, the consolidated financial statements for the year ended December 31, 2010 give a true and fair view of the financial position, the results of operations and the cash flows in accordance with International Financial Reporting Standards (IFRS).

KPMG AG



John A. Morris



François Rouiller

Basel, January 26, 2011