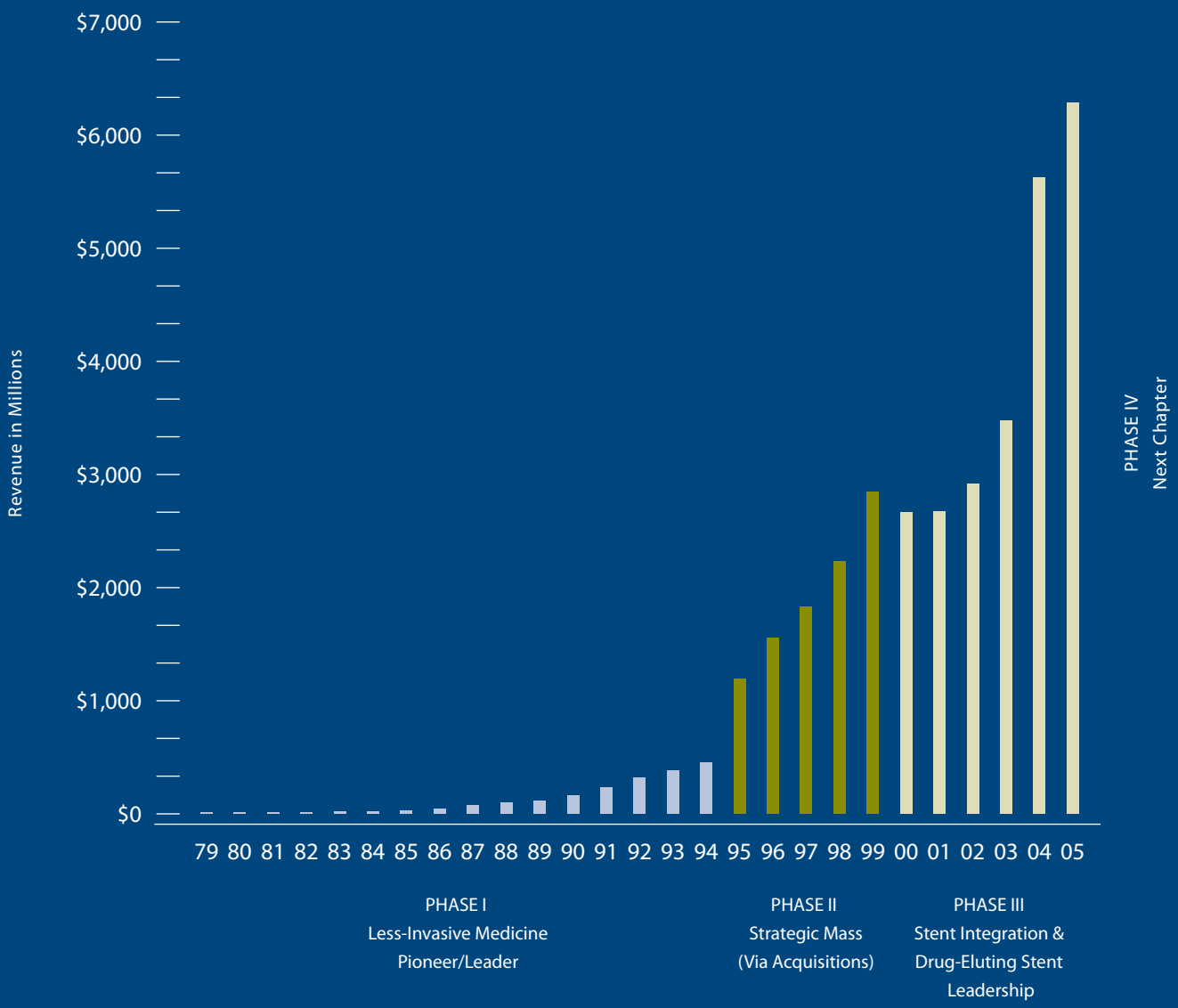
There are millions of reasons
we set such high standards for everything we do.

Boston Scientific
Delivering what's next.™



FROM PIONEER TO LEADER

Boston Scientific has achieved an impressive compound annual growth rate of more than 35 percent over the past 26 years. Our rapid rise as an innovator and acquirer has brought us to a powerful leadership position, with more than 80 percent of our sales from market-leading products sold in the markets we serve. The high standards that have enabled us to achieve this success are the key to our future.

Annual Report 2005

To Our Shareholders and Employees

The year 2005 was a time of great change in the medical device industry. Mergers and acquisitions continued at a quickening pace, and new innovations reshaped the medical landscape. But perhaps the year's most noteworthy theme was the public's growing concern with the way our industry generates and shares information about drugs and devices. This concern, which has been heightened by high-profile lawsuits and revelations about editorial practices in reporting clinical trial findings, means that the standards a company uses to run its business take on greater importance than ever. At Boston Scientific, we see the question of standards as a scientific requirement and an ethical imperative. As this Annual Report makes clear, the primary motivation for the standards we use to guide our actions is the patient – every person whose life is touched by one of our products.

The past year will also be remembered for our proposal to acquire Guidant Corporation. This proposed acquisition is a natural outgrowth of our strategy to diversify our business and accelerate our growth, a strategy that the board and senior management of Boston Scientific is committed to pursuing for the long run. Our companies would combine the resources of two of the leading innovators in cardiovascular medicine and expand our reach into the rapidly growing cardiac rhythm management (CRM) market. We believe that Guidant's life-saving heart failure technologies will be one of the most exciting areas in medical devices over the next decade, so this proposed acquisition gives us a significant strategic presence in a crucial market. It also makes Boston Scientific a pre-eminent medical device company, with total anticipated 2006 revenue of nearly $9 billion.

Beyond complementary market strengths, Boston Scientific and Guidant share a proud, common heritage as healthcare pioneers with a global reach, as well as a core commitment to advancing medical science and providing better patient care. For all these reasons and others, we feel confident that this proposed acquisition will be a transformative event for Boston Scientific, and will shape the Company for years to come. We enthusiastically welcome Guidant employees as we begin writing the next chapter in our history together.

Along with our expansion in the medical device marketplace, the growing complexity of our products and the increasingly global nature of our business bring a continuing responsibility to implement long-term improvements in our quality compliance systems. On January 25th of this year, Boston Scientific received a Corporate Warning Letter from the U.S. Food and Drug Administration (FDA) raising a number of issues with respect to our quality compliance systems. We understand the seriousness of the issues raised by the FDA. As our initial response to the agency makes clear, we are committed to improving our quality compliance systems at all Company facilities and intend to keep the FDA fully informed of our progress through frequent communication. Our response to the FDA is an important step in that dialogue and underscores our commitment at all levels of the Company to comprehensively address each quality systems issue identified by the agency.

Jim Tobin
President & Chief Executive Officer

Pete Nicholas
Chairman of the Board

While we intend to address all the issues cited by the FDA, we must go further and make permanent improvements to ensure we have first-class quality systems. That is why we established Project Horizon, a global, cross-functional quality systems re-engineering effort that is the number one project across the Company. The Board of Directors is actively monitoring this effort and recently formed a new committee to assess the Company's progress in responding to the FDA's concerns and in meeting our overall quality compliance systems objectives.

Continuing to Set the Standard in Clinical Science

While the Guidant acquisition was the most dramatic announcement of the year, we also marked a number of other significant achievements throughout the organization in 2005. In our first full year of selling our TAXUS® Express²™ paclitaxel-eluting coronary stent system in the U.S., we maintained our leading market share, despite intense competition. This leadership position has helped contribute to 2005 total sales of $6.28 billion, a 12 percent increase over 2004.

"This leadership position has helped contribute to 2005 total sales of $6.28 billion, a 12 percent increase over 2004."

In clinical trials, clinicians and regulatory groups hailed our new SYNTAX trial. This global trial is designed to determine the best treatment for complex coronary disease (obstructed or narrowed arteries in both the left and right sides of the heart) by randomizing patients to receive either the TAXUS stent system or coronary artery bypass graft treatment. We believe that this trial, which is currently enrolling patients, will help to ensure that valuable information about the limits and cost-effectiveness of drug-eluting stents is captured and shared with cardiologists, so that it can inform their clinical practice.

Among other trials, we welcomed results from the independent, multicenter STENT registry, which further supported the efficacy and safety of the TAXUS stent system among real-world patients with blocked coronary arteries. Nine-month sub-population data from the TAXUS V clinical trial also provided important and positive data on the performance of the TAXUS stent system for the treatment of coronary artery disease in higher-risk patients, including those with small vessels, long lesions and diabetes.

Today, the TAXUS stent system has established an outstanding long-term safety and efficacy record as demonstrated by four years of clinical data.

In the important new area of carotid stenting, we presented data from the BEACH clinical trial. This trial demonstrated that our Carotid WALLSTENT® Monorail® Endoprosthesis, used in combination with the FilterWire EX® and FilterWire EZ™ Embolic Protection Systems, improves blood flow within the carotid artery, and that the artery was still open one year post-procedure in patients at

high risk for the traditional surgical procedure known as carotid endarterectomy. These devices independently carry the CE Mark and are commercially available in Europe and other international markets, where they are market leaders. We anticipate U.S. approval of these products in 2006.

Achievements Across the Company

In our Cardiovascular Group, total sales were $4.91 billion in 2005. Worldwide coronary stent system sales were $2.69 billion in 2005, a 15 percent increase over 2004. In Europe and other international markets, we launched the TAXUS® Liberté™ paclitaxel-eluting coronary stent system, the world's first second-generation drug-eluting stent. The improved deliverability of the TAXUS Liberté stent system has led to an enthusiastic reception among physicians, who judge it to be a significant advance in drug-eluting stent platform technology for a more complex coronary anatomy. We recently submitted to the FDA the final module of our Pre-Market Approval application for the TAXUS Liberté stent system and look forward to its U.S. launch.

In other highlights, we announced the opening of our new Maple Grove, Minnesota, research and development facility in October. We also announced the TAXUS Stent Assurance Program, which provides participating medical centers – at no additional charge – a TAXUS stent system if a patient requires a re-intervention due to in-stent restenosis or re-blocking of treated arteries.

In our Neurovascular business, the FDA granted a Humanitarian Device Exemption approval for our Wingspan™ Stent System with the Gateway™ PTA Balloon Catheter. The Wingspan Stent System is designed to open blocked arteries in the brain, and is currently the only approved device available in the U.S. for the treatment of intracranial atherosclerotic disease (ICAD). We also announced the U.S. launch of our Matrix²™ 360° Detachable Coils, which have been cleared by the FDA for the treatment of high-risk or inoperable brain aneurysms. The Matrix² 360° Detachable Coils feature a new 360-degree shape designed to allow conformability and uniform distribution within intracranial aneurysms.

"In our Cardiovascular Group, total sales were $4.91 billion in 2005. Worldwide coronary stent system sales were $2.69 billion in 2005, a 15 percent increase over 2004."

Our Endosurgery Group, which continues to be the world leader in endoscopic surgical technologies, grew 13 percent to $1.23 billion in 2005, enjoying considerable expansion across all its businesses and launching several new products.

Within Endosurgery, our Endovations™ Endoscopy Systems team continued to make progress toward the development of the first single-use endoscope platform for colonoscopies. This platform includes a digital, fully integrated console and image capabilities that we believe will be uniquely

differentiated from the reusable endoscope. By offering predictable performance and eliminating the need for reprocessing and standard scope repairs, the Endovations Endoscopy System is designed to provide a more efficient alternative for healthcare providers and potentially enhanced information management for the clinician.

Our Neuromodulation Group posted significant growth in 2005 in both its Auditory and Pain Management businesses, and contributed $148 million in sales during its first full year as part of Boston Scientific. In addition to its established commercial platform with cochlear implants, the group launched the Precision® Spinal Cord Stimulation System in the U.S. in April and received the CE Mark in Europe in August. This technology, the world's smallest and first rechargeable spinal cord stimulation system, uses electrical stimulation to mask pain signals as they travel through the spinal cord to the brain. The Precision system has been well received as a new option for the treatment of chronic pain and has already brought relief to thousands of patients.

In 2005 alone, the Company registered 267 new patents, for a total of 4,106, as well as 101 FDA product approvals and clearances and 26 CE Marks. Throughout the year, we continued to support high standards in medical device policy. Our Government Affairs and Reimbursement and Outcomes Planning teams advocated for policy changes in labeling provisions for reprocessed devices, contributed to passage of legislation to provide abdominal aortic aneurysm (AAA) screening for the elderly in the United States and supported higher Medicare payment for complex drug-eluting stent (DES) cases.

The year also saw a number of awards that acknowledged our efforts in the medical device industry. *IndustryWeek* presented the 10 Best Plants in North America award to our Wayne, New Jersey facility, which is a leading producer of highly engineered grafts and fabrics used to repair blood vessels. *Logistics Management* magazine chose Boston Scientific for its 2005 Best Practices in Logistics Management Gold Award to recognize our successful efforts in increasing global supply chain efficiency for our TAXUS® stent system. J.D. Power & Associates recognized our Quincy, Massachusetts distribution center for call center customer satisfaction excellence, based on its outstanding performance handling more than 1.4 million customer communications annually. Finally, *Fortune*® selected us for its America's Most Admired Companies and 100 Fastest-Growing Companies lists for 2005.

Looking ahead, we believe we have the ability to deliver sales growth across the Company, in our existing franchises as well as in our new business opportunities such as neuromodulation and cardiac rhythm management. This is particularly true of our international operations, where sales grew an impressive 15 percent in 2005. We are especially pleased with year-over-year TAXUS stent system sales growth, which increased 38 percent despite new competition.

Setting Our Sights on the Future

We reported to you last year that our strategic plan sets the stage to realize our substantial potential. We continue to pursue and make progress against this plan, which includes several priorities:

Accelerate profitable base-business growth. As we reported above, many of our key divisions achieved double-digit growth rates in 2005. In addition, we continued to derive strong revenue from number-one market share positions. In the markets we serve, 90 percent of our interventional cardiology sales and 75 percent of our endosurgery sales came from market-leading products.

Invest to expand drug-eluting stent (DES) market share and fortify our leadership. This remains a central priority for us around the world, including regions such as Japan, where we expect that the TAXUS® stent system will become commercially available during the first half of 2007. By 2008, we expect to see more than $1 billion in new market growth from drug-eluting stents, in part from novel stent delivery systems and geometries, stents for expanded indications and stents made from next-generation materials.

Deliver on 'game changer' products and markets. We anticipate, with FDA approval in the second half of 2006, that our Carotid WALLSTENT® Monorail® Endoprosthesis in conjunction with our FilterWire EX® and FilterWire EZ™ Embolic Protection Systems, will be a driver of growth in our peripheral interventions business for the next several years.

Build new scale beyond catheter/stent platforms. The most obvious examples of our progress against this priority are the Neuromodulation Group and the new Cardiac Rhythm Management Group. Guidant holds the number two position in the overall CRM market, which is growing an average of 12 percent annually to an estimated $12.80 billion a year by 2008. Guidant was the original creator of the implantable cardioverter defibrillator (ICD) and the resynchronization therapies that stem from it. Guidant also adds a cardiac surgery business to our Cardiovascular Group, as well as a second drug-eluting stent program, the XIENCE™ V everolimus-eluting coronary stent system. These technologies provide a highly attractive growth platform to scale beyond our current businesses.

Other investments we made in 2005 that expand our technology portfolio include: endoscopic stent technologies acquired from Willy Rusch GmbH, which offer new treatment alternatives for patients with esophageal and tracheo-bronchial obstructions; Advanced Stent Technologies, Inc., which develops stents and stent delivery systems specifically designed to address the unique anatomical needs of coronary artery disease in bifurcated vessels; Rubicon Medical Corporation, a developer and manufacturer of interventional embolic protection devices; and CryoVascular Systems Inc., which has developed a proprietary technology known as the PolarCath™ Peripheral Dilatation System, which uses liquid nitrous oxide to provide precise cooling of a diseased peripheral artery during balloon angioplasty.

Continuously improve the efficiency and effectiveness of our organization. To improve our efficiency, we are pursuing several lean product development, performance management and expense control initiatives. But as we have mentioned above, quality remains our highest priority. In addition to the new Board committee created to monitor our quality efforts, we have named a new Vice President of Program Management to lead Project Horizon, our quality system re-engineering effort. In addition, we have appointed a cross-functional team of nearly 100 people to help change our approach to quality and compliance in critical business processes. Project Horizon is already establishing the quality platform that will support the next stage of our growth, and it is operating at virtually every level of the Company. It is up to everyone at Boston Scientific to assume personal responsibility for maintaining the highest possible quality standards in everything we do.

A Shared Commitment

We take great pride in the generosity exhibited by Boston Scientific employees in response to several natural disasters in 2005. Our employees made a substantial donation to the Red Cross in support of relief efforts for the Asian tsunami. When hurricanes struck the Gulf Coast region, Boston Scientific employees gave their time and money to aid those affected by the destruction. The Company and its employees donated nearly $4 million to the Red Cross and to Doctors Without Borders for efforts related to natural disaster relief. We were honored to receive an American Red Cross Circle of Humanitarian Award on behalf of all our employees and their families who generously contributed their time and financial resources to help those in need. To expand our impact among underserved patients in communities where we are located, the Boston Scientific Foundation contributed more than $1 million to charitable organizations. This generosity speaks to our collective commitment to improving lives wherever help is needed and to what it means to be part of Boston Scientific.

Within our organization, we wished Jim Taylor well as he retired from his position as Executive Vice President for Operations. In his six years with the Company, Jim revolutionized our manufacturing capabilities and brought us to a new level of performance in operations and supply chain management. Among his many contributions, Jim led initiatives that realized significant savings in operations, which helped us fund the development of the TAXUS® stent program.

We made three key senior management appointments to our international team. Dan Moore was promoted to President of Inter-Continental. Ged Wallace, a 27-year industry veteran, became President of Boston Scientific Europe. And David McFaul was promoted to President of Boston Scientific Japan.

We also named a leadership team for our new Cardiac Rhythm Management Group. The team consists of Mark Bartell, former President of U.S. Sales Operations for Guidant; Fred Colen, currently Executive Vice President and Chief Technology Officer for Boston Scientific; and

William McConnell, former Vice President and Chief Information Officer for Guidant. This group of seasoned leaders will report to Jim Tobin. In our new Cardiac Surgery business, which also comes to us as a result of the Guidant acquisition, we welcomed Maria Degois-Sainz, who continues in her role as President and will also serve on an interim basis as President of Europe for the Cardiac Rhythm Management Group.

We have invited two Guidant board members to join the Boston Scientific Board of Directors. Nancy-Ann DeParle is a Senior Advisor to JP Morgan Partners, LLC, and previously served as the Administrator of the Health Care Financing Administration (HCFA) (now the Centers for Medicare and Medicaid Services). Dr. Kristina Johnson is Dean of the Pratt School of Engineering at Duke University and a former professor in the Electrical and Computer Engineering Department at the University of Colorado at Boulder.

In closing, we would like to reiterate our welcome to the nearly 8,000 Guidant employees who will be joining the Boston Scientific family. Although our companies have grown significantly, in many ways we've both retained the spirit of a smaller organization – one that values initiative and creativity, and one that recognizes each person's talents and contributions. Like Guidant, Boston Scientific is a place for people who want to make a difference. We hope you are as excited as we are about the enormous potential of the new Boston Scientific.

We will continue to hold our actions to the highest quality and ethical standards and strive for transparency and openness in everything we do. Patient well-being has been our principal concern for more than 25 years, and as we work each day to help improve life through medical technology, we look forward to the support of employees and customers – of both Boston Scientific and our future colleagues at Guidant – to help us realize the many opportunities before us and build on the considerable progress we have made to deliver what's next.

Thank you for your belief in and continued support of our mission.

Sincerely,

Jim Tobin
President and Chief Executive Officer

Pete Nicholas
Chairman of the Board

March 28, 2006

REASON

81,476

Because in our industry, higher standards
can transform a patient's life – and a company's future.

Kathleen Thompson is a recipient of a TAXUS® Express²™ paclitaxel-eluting coronary stent system, which is supported by the most comprehensive set of randomized, controlled clinical data available on drug-eluting stents.

At Boston Scientific, higher standards are an absolute necessity. A scientific requirement. And an ethical imperative.

In newspapers and online chat rooms, courtrooms and public hearings, hospitals and clinics, healthcare industry standards are talked about more today than ever before. People are questioning the practices of drug and device companies, and even the science behind the medicine. As a global leader in the medical device industry, Boston Scientific must be an active participant in this discussion.

A researcher working in a lab at our Natick, Massachusetts, headquarters.

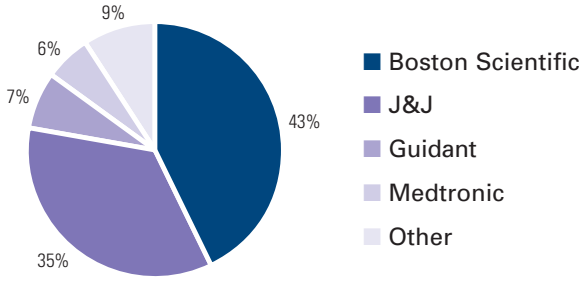
Because our mission is to improve the quality of patient care, we must make patient safety the primary consideration in everything we do. Because the products and evidence we provide influence treatment guidelines, we must work to give clinicians broad, in-depth information for decision making. Because we are a business in a highly competitive industry with inherent risks, we must drive ourselves to do everything we do, better.

At Boston Scientific, we're constantly looking to set higher standards for ourselves and our industry. By conducting clinical trials with scientific rigor. By providing more objective, complete information to clinicians and their patients. And by pursuing new levels of excellence in every area, from research and development to quality and compliance.

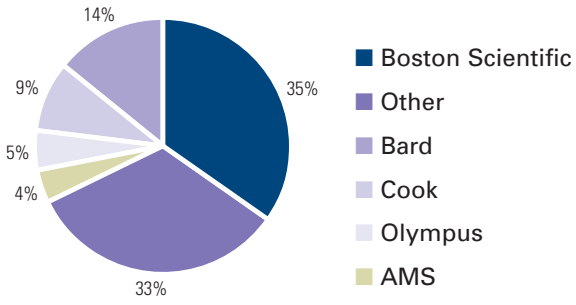
In our industry, there's nothing easy about setting higher standards. But it's always easy to remember why we must try – because the lives of millions of patients worldwide can be dramatically improved if we do.

THE STANDARDS OF GLOBAL MARKET LEADERSHIP

With outstanding execution by our sales force, our acquisitions and strategic alliances combined with our internal R&D programs have resulted in a market leadership position in nearly all the markets we serve.



Interventional Cardiology



Endosurgery

Source: Boston Scientific internal estimates based on 2005 sales.

REASON

274,032

Because clinical trials must be rigorous and daring enough to reflect the real world.

Ron Meddings is enrolled in the BEACH clinical trial, and received the Carotid WALLSTENT® Monorail® Endoprosthesis. This investigational device is recommended for patients at high risk for surgery. Ron underwent this minimally invasive stenting proceedure after previous surgeries failed to treat his carotid artery disease.

The real world is complex. Every patient is different.

That's why our clinical trials examine the most complex patients and procedures.

Because that's the world we live in.

The rapid evolution of medical technology is giving clinicians and their patients more treatment options all the time. These new products and procedures require clinical trials to determine safety and efficacy and to obtain regulatory approval. Designed, performed and reported correctly, clinical trials offer important opportunities to test product performance, inform the guidelines clinicians use to make treatment decisions and ultimately advance the practice of medicine to improve outcomes for patients.

But the increasing volume and variety of trials, data and their claims can actually make it more difficult for clinicians to make informed decisions. Trials vary in terms of scientific rigor and data quality. Furthermore, medical device trials can be complex and difficult to interpret, in part because the human factor presented by individual technique in implanting or using a medical device can strongly affect the results.

Fortunately, standards are emerging that can help clinicians and patients judge the quality and significance of clinical trials. In 2005, a new scale for ranking drug-eluting stent clinical trials was created: the Silber Score. This new scale, one of several approaches to assessing the quality of data, offers a valuable tool for clinician decision making. We're proud that Boston Scientific's stent trials have consistently scored higher than the industry average on the Silber Score. (See the sidebar on the right.)

Boston Scientific has been setting high standards for scientific rigor in the way we design and conduct clinical trials. The groundbreaking, wide-ranging clinical program supporting our TAXUS® Express²™ paclitaxel-eluting coronary stent system is an excellent example, delivering the industry's most comprehensive set of randomized, controlled clinical data on drug-eluting stents. The data we released in 2005 from our TAXUS V trial gave clinicians answers to critical questions about stent use for some of the most complex lesions, procedures and patients.

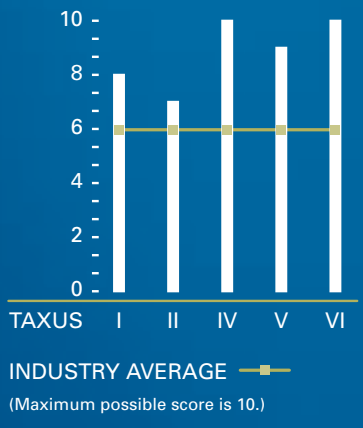
The TAXUS® stent program continues to set higher standards for clinical science with the SYNTAX clinical trial. SYNTAX takes a revolutionary approach to informing real-world drug-eluting stent use by recruiting patients with no exclusion criteria. Exclusion criteria can sometimes be misused to exclude patients less likely to generate positive data for a trial. As a result, the trial has the potential to explore the limits of drug-eluting stent therapy – and expand our knowledge about intervention for the broadest range of patients. SYNTAX is currently in the patient enrollment phase. The rapid success of our recruitment efforts (1,100 patients across 70 sites in just 12 months) has shown how committed we are about pursuing this important research, and how successfully we are able to collaborate with our clinician partners.

Boston Scientific has set other high standards for monitoring product safety. Patient safety is our foremost concern, and to demonstrate our commitment to that, we expanded the scope of our Global Safety Office to include patient safety monitoring across the entire product life cycle. This team continuously monitors the quality of data, the completeness and detail of information we make available and the safety of patients across our clinical trials and following commercialization. Beyond clinical trial design, our Clinical Sciences team is also developing new, more sensitive methods for testing our products in pre-clinical and clinical trials, from novel ways to measure local drug release to new methods for studying the effects of implanting multiple stents.

A NEW STANDARD FOR EVALUATING CLINICAL TRIALS

The multitude of clinical trials and real-world registries often makes it difficult for clinicians to know which data they can rely on in making treatment decisions. To help clinicians evaluate and compare drug-eluting stent trials, Prof. Sigmund Silber, M.D., F.A.C.C., F.E.S.C., has established the Silber Score. Trials are evaluated objectively, based on a transparent checklist of key parameters, such as clearly defined endpoints, proper sample size, blinding, multi-center operation, full accounting of patients and independent analysis.

As Dr. Silber has noted, "Boston Scientific is conducting the type of clinical trials that are consistent with the strict scientific criteria that physicians need to consider when evaluating their impact on the decision-making process for their patients." Feedback such as this and leading scores on Dr. Silber's trial rankings highlight our commitment to setting new standards for scientific rigor in clinical science.



** Dr. Silber's work developing the Silber Score has been funded by TCTMD.com's Evidence-Based Medicine Center, which is supported by an unrestricted grant from Boston Scientific.*

REASON

456,098

Because better medical information helps clinicians and their patients make better decisions.

Nicholas Cardellechio suffered with the symptoms of benign prostatic hyperplasia (enlarged prostate) and was treated with the Prolieve Thermodilatation® System, one of the Endosurgery Group's latest technologies.

Today, there is a flood of medical information.

It makes it difficult to tell what's accurate, impartial and complete.

It makes transparency and honesty more important than ever.

Recent events have caused concern about the integrity of information provided by companies in the medical industry. The issues have ranged from selective disclosure of clinical trial data to the questionable ghostwriting of journal articles. These events threaten to erode the public trust and spawn the suspicion that companies in our industry are more interested in market share than medical science.

The public has a right to expect truth, transparency and openness when it comes to information they and their doctors rely on to make healthcare decisions. At Boston Scientific, we endeavor to disclose all significant clinical information to clinicians as quickly as possible and to maintain the highest standards for providing it. This means pursuing a commitment to clinical trials that goes far beyond what's expected or required, and giving clinicians access to comprehensive clinical trial results – whether they are favorable to our product or not. It means maintaining a clear distinction between marketing and science while pursuing both aggressively. It means training clinicians in new procedures regardless of whether they purchase our products to perform those procedures.

We're also setting higher standards for the quality of the information we provide. A prime example: meta-analysis of pooled clinical trial data. Commonly, clinical data is analyzed only within the context of a single trial. Boston Scientific has established a new global data monitoring committee tasked with looking across all of our clinical studies. By combining the results of multiple, related studies, this committee is able to uncover low-frequency events that wouldn't be noticed within any one study. Analyzing pooled data this way requires consistent methods and data quality from trial to trial. It also requires consistent and reliable definitions of terms. We've been standardizing terms and procedures across all our trials because we believe that doing so influences how well physicians can understand what clinical results actually mean for real-world outcomes.

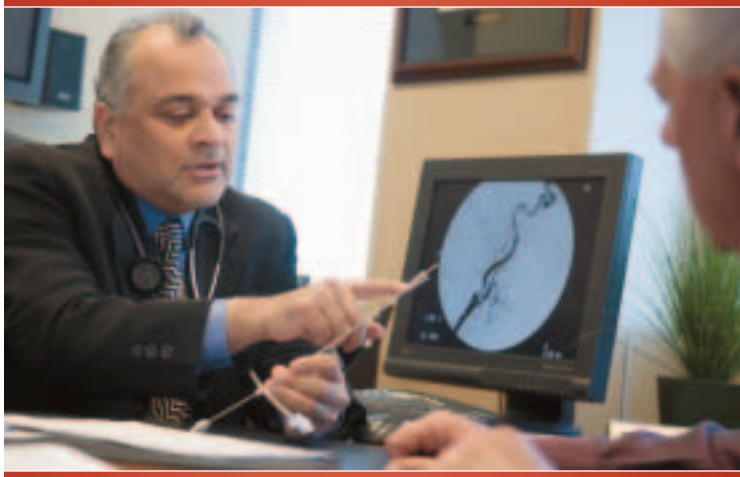
Boston Scientific sets such high standards for medical information for several reasons. First, we know the information we provide is informing the development of medical treatment guidelines used by clinicians around the world, such as those of the European Society of Cardiology for coronary artery disease. Second, to succeed as a medical innovator, we must be known as a trustworthy source of information and products. Finally, clinicians must see us as trusted partners and collaborators, and believe that the information we provide about our products will help them make the best decisions for their patients.

High Standards for Information from Start to Finish

High-quality information plays a critical role from the beginning of a product's design to its eventual use by clinicians performing procedures. Industry, clinical and disease-state information drive innovation in product research, development and design. Information in the form of manufacturing best practices and quality standards ensures that every device meets performance and safety requirements. Finally, there is a critical transfer of information that must take place between clinicians and their patients, which helps inform important decisions about treatment options.

Research and development in Maple Grove, Minnesota.

Quality testing at our Neuromodulation Group facility in Sylmar, California.



Dr. Subbarao Myla discussing carotid stenting with his patient, Ron Meddings.

REASON

736,089

Because someday,
innovation will spread faster than disease.

Jana Gersten, who experienced extreme chronic pain due to a wrist injury, was implanted with the Precision® Spinal Cord Stimulation System.

If your mission is to improve patients' lives,

no amount of effort is too much.

And it's a journey that never ends.

At Boston Scientific, our commitment to setting higher standards for ourselves continues far beyond clinical science and medical information. In every area, from innovation to quality, from day-to-day operations to long-term enterprise building, we're continuously setting the bar higher for ourselves.

A Never-Ending Focus on Quality

We are always working to achieve higher quality across every process, from product development and manufacturing to distribution and customer service. We take our recent quality problems cited by the FDA very seriously, and we are committed to resolving them. The FDA's mission to protect the public health demands nothing less, and we must demand nothing less for our Company and the customers we serve.

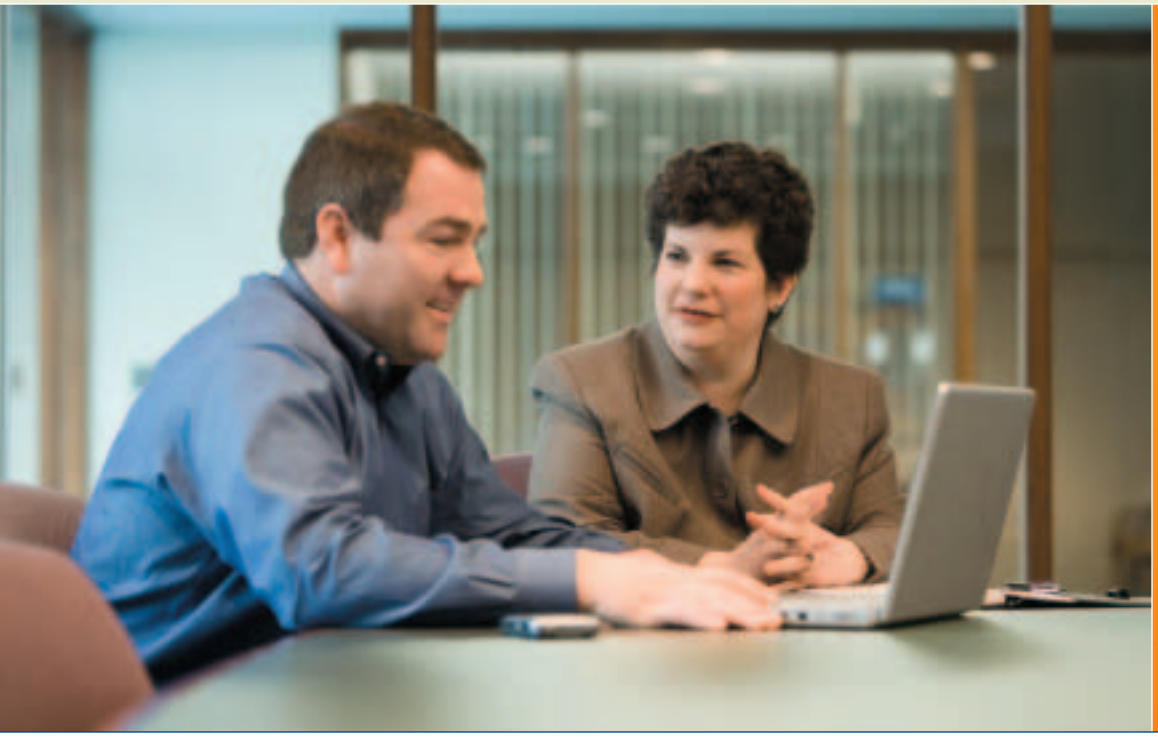
As part of our dedication to continuous improvement, in 2005 we undertook a company-wide quality initiative called Project Horizon. This initiative is designed to build a quality platform to sustain us for the next phase of our growth, and will help us to better support our customers and benefit patients. We're using a top-level, cross-functional approach led by business and quality professionals to design a program that everyone at Boston Scientific can commit to and take responsibility for. We've formed a new committee of the Board of Directors to focus on quality, as part of our work to establish a long-term master plan for quality compliance excellence.

BUILDING OUR NEXT-GENERATION QUALITY PLATFORM

Boston Scientific's Project Horizon initiative is taking our company-wide commitment to quality and compliance to the next level.

Project Horizon's objectives include:

- Making it easier for clinicians to report problems and product complaints and for Boston Scientific to respond more effectively
- Improving the process to make rapid and accurate decisions as to whether a situation warrants action
- Standardizing and enhancing the information our senior management receives from early warning systems
- Harmonizing and upgrading the process by which we capture, investigate, learn from and prevent future occurrence of problems
- Ensuring that manufacturing processes are fully validated with state-of-the-art standards for control and quality within strict specifications
- Achieving high standards of quality in the software that controls our manufacturing equipment, as well as software embedded in our products
- Finding new ways to qualify our third-party suppliers, and to ensure that they are using quality approaches that are up to our standards
- Ensuring that we can track and manage our products throughout their life cycle once they leave our facilities, for full assurance of customer and patient safety
- Revamping our approach to training to ensure that employees have the knowledge and qualifications required to perform at the highest level of quality



Brian Burns, Senior Vice President for Quality, and Joanna Engelke, Vice President, Program Management, at work on the Project Horizon quality initiative.

Delivering on the Promise of Innovation

For years now, we've aspired to set new standards for innovation with our hybrid innovation strategy of investing in internal research and development as well as making acquisitions and strategic alliances. Using this approach, we've invested nearly $6 billion in new technologies over the past five years.

We're also applying powerful Six Sigma methods to product development. For example, we have formalized a process called "Voice of the Customer" which proactively solicits customers' input and recommendations to better understand their current and future clinical needs. We then incorporate their insight into product designs and throughout the development process. By using multiple tools to solicit input from customers, we can more successfully design innovative, differentiated products that better meet clinician needs. We also strive to lead the way in another innovation process: designing for robust quality. We are applying advanced analytical, statistical and experimentation techniques to build higher performance and quality into new products and concurrently into their manufacturing processes. These methods can help us achieve new levels of quality, customer satisfaction, productivity and profitability.

We continue to take advantage of Boston Scientific's broad technology portfolio to spread successful innovation from one therapeutic area to another. For example, we're working to apply our drug-loading stent technology to new areas, such as a drug-loaded ureteral stent designed to improve clinical outcomes following stent placement. As another example, we're exploring the use of our drug-elution technology in cochlear implants to help preserve a patient's residual natural hearing.

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Researchers in Maple Grove, Minnesota, working on our TAXUS® paclitaxel-eluting stent system program.

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POWERFUL PRODUCT AND GROWTH POTENTIAL

From groundbreaking innovations to continuous improvement of existing products, we're focusing on an extremely varied pipeline with short-term and long-term promise. Here are just a few of the highlights.

Growing our base businesses
Boston Scientific is maintaining solid growth and profitability across a broad and healthy base of franchises in multiple medical specialties – from endoscopy to neurovascular stenting, women's health to urology. In fact, 90 percent of our interventional cardiology sales and 75 percent of our endosurgery sales came from leading products in the markets we serve.

Maintaining and expanding our drug-eluting stent leadership
We have retained our leading position in drug-eluting stents and expanded the market. 2005 saw the successful launch in international markets of the TAXUS® Liberté™ paclitaxel-eluting coronary stent system, designed to offer improved deliverability and conformability in challenging anatomy. We have completed our Pre-Market Approval application for the TAXUS Liberté stent system to the FDA. We expect to launch the TAXUS Liberté stent system in the United States during the second half of 2006, pending regulatory approval. Beyond the TAXUS Liberté stent system, our drug-eluting stent pipeline is continuing to develop as we explore new stent designs, new materials and new delivery systems – as well as the first device specifically designed to address the challenges of arterial bifurcations with drug-eluting stent technology.

Pursuing game-changing technologies
Bold innovations that can make a dramatic impact on standards of care offer us significant opportunities for growth and market share, but they also involve greater risk: they take longer to develop and they don't always succeed. One example of a game-changing technology is our Endovations™ Endoscopy System – a revolutionary, integrated digital system that may offer clinicians a single-use endoscope and potential for procedural efficiencies in colonoscopies. We anticipate the first human use trial of Endovations in the second quarter of 2006.

We are awaiting FDA approval of the Carotid WALLSTENT® Monorail® Endoprosthesis, used in combination with the FilterWire EX® and FilterWire EZ™ Embolic Protection Systems, for carotid stenting and embolic protection. This combination of acquired technology with internal research and development is an excellent example of our hybrid innovation strategy in action, and is the market-leading carotid stenting and embolic protection system in Europe.

Broadening our footprint
We've been moving successfully into areas beyond catheter and stent-based technologies. Exciting and new microelectronic technologies from our Neuromodulation Group are exceeding expectations and offering excellent revenue potential. Once approved, we believe the Harmony Cochlear Implant System will offer the greatest capability of any system on the market today. Scheduled to be introduced in 2006, it is the first and only system that can deliver music, improved sound quality and better speech perception for people with hearing loss. Developed to assist patients in reaching their maximum hearing capacity, this upcoming product release has the potential to expand our Auditory business.

The Precision® Spinal Cord Stimulation System for advanced pain management was launched in 2005 for treating chronic pain and already is delivering approximately $100 million a year in annualized revenue.

A clinical trial is currently underway to evaluate the safety and efficacy of occipital nerve stimulation as a treatment for refractory migraine headache. The study, known as PRISM (PRecision Implantable Stimulator for Migraine), will use the Precision system and involves approximately 150 patients at up to 15 sites in the United States. The Precision system, the smallest rechargeable neurostimulator on the market today, will be used to deliver electrical impulses to the occipital nerves located just under the skin at the back of the neck. Occipital nerve stimulation is intended to treat migraine headache in patients who do not respond to other therapies. There are more than 28 million migraine sufferers in the United States and up to 10 percent of these patients may not respond to existing treatments.

The TAXUS Liberté paclitaxel-eluting stent system and the Carotid WALLSTENT Endoprosthesis in combination with the FilterWire EX and FilterWire EZ Embolic Protection Systems are not available for sale in the United States.

Achieving Operational Excellence

We've applied continuous improvement to all elements of our manufacturing process, aiming to be even better than Six Sigma process capability, a notably high standard. Our results are meticulously measured and monitored. Continuous improvement initiatives resulted in greater than 10 percent savings annually in the cost of production (with 2004 as the base year), and a gross margin of 78 percent in 2005. Over the last three years, we've reduced the time it takes to manufacture products by 9.4 percent and improved plant inventory turns by 14.8 percent. Plant inventory turns measure how quickly a manufacturing site procures, builds and ships its inventory.

We've also achieved greater flexibility to respond to today's competitive marketplace. We've developed production lines that can accommodate quick changes between product families to meet changing demand levels and product mix. We've implemented an efficient global product labeling system to meet the demands of country-specific labeling. At the end of 2005, we began implementing a new global supply chain strategy that will allow us to predict and respond to customer demand better and to reduce inventory levels. In 2005, we also expanded our ability to serve our international markets by opening a new, 250,000-square-foot distribution center in Kerkrade, The Netherlands.

Nurturing the Talents of Our People

The competitive market in which we work and the leadership position we enjoy demand that our employees meet the highest standards at every level, in every function, around the globe. In 2005 we focused on improving the performance, accountability, management and benefits of our employees.

Our efforts are aimed at ensuring that we are attracting, rewarding and retaining our highest performers. We're also enhancing and developing our management team to keep up with the complexity and the scope of our fast-growing business. This includes training and developing general managers to become better evaluators of talent in current and prospective employees.

Acquisitions provide a frequent opportunity to bring in talent from other organizations, industries and geographies. They also present significant challenges, such as the need to fill new kinds of positions as we move into new technologies and treatment areas. We're focused on improving our ability to integrate companies in ways that deliver the most benefits – for us and our customers.

Building a Stronger Enterprise

The strategic and creative way Boston Scientific has approached mergers and acquisitions has established new standards for the whole industry. It's been a key part of our success since our early years, and we believe it can be our most powerful tool for achieving continued diversification and growth.

Our acquisition of Advanced Bionics in 2004 demonstrated the transformative power of our approach. It gave us a strong entry into the new and extremely promising area of neuromodulation – both its advanced technology platforms and the diverse clinical challenges it has the potential to address. Boston Scientific's strengths are now being applied to Advanced Bionics, complementing its technology with our capabilities, such as international sales and distribution.

Although Boston Scientific has a proven track record of successful integrations, we realize we don't have a monopoly on good ideas. Our transition and integration planning are guided by fundamental principles: a spirit of collaboration, open communication, a desire to combine the best practices of both organizations, rapid identification and retention of top and high potential talent and a process to introduce new employees to Boston Scientific's practices and culture.

AN ACQUISITION THAT COULD RESHAPE THE INDUSTRY

On January 25, 2006, we entered into a definitive agreement to acquire Guidant Corporation. Guidant develops, manufactures and markets products that focus on the treatment of cardiac arrhythmias, heart failure and coronary and peripheral disease.

The acquisition will enable us to become a major provider in the high-growth cardiac rhythm management business, which will significantly diversify our revenue stream across multiple business segments and enhance our overall competitive position. In addition, Abbott has agreed to acquire Guidant's vascular intervention and endovascular businesses and will share with Boston Scientific the drug-eluting stent technology it acquires from Guidant. This will enable us to access a second drug-eluting stent program that will complement our existing TAXUS® stent program.

The transaction is subject to customary closing conditions, including clearances under the Hart-Scott-Rodino Antitrust Improvements Act and the European Union merger control regulation, as well as approval of Boston Scientific and Guidant shareholders. Subject to these conditions, we currently expect the acquisition to close in April, 2006.

This is a bold move, and one that reflects a long history of transformative acquisitions at Boston Scientific. Given the strong pipelines and powerful market positions both companies bring to the table, we're confident that this acquisition will allow us to deliver strong shareholder value in the coming years. It's an exciting time for Boston Scientific.

REASON

943,786

Because every positive outcome could
lead to a million more.

Michelle Tjelmeland and her daughter Ellie both enjoy restored hearing with cochlear implants developed by Boston Scientific's Auditory business.

When you have the power to improve lives,

you have to share it.

In any way you can.

Our mission drives us to seek even more ways to improve lives. We're pursuing higher standards for the way we contribute to the communities where we live and work. Through the Boston Scientific Foundation and other philanthropic efforts, we make significant financial contributions – and dedicate time, effort and personal commitment – each year. The Foundation's mission is to support education and healthcare initiatives that target the underserved and those at risk. It gives priority to initiatives that target a clearly defined community or population and that have a strong potential to produce measurable long-term improvements in healthcare and education. To maximize local impact, employee volunteers in each region where Boston Scientific is located direct and drive the Foundation's activities.

We take great pride in the generosity exhibited by our employees in response to several natural disasters. We began the year with a substantial donation to the Red Cross in support of relief efforts for the Asian tsunami. When hurricanes struck the Gulf Coast region, Boston Scientific employees gave their time and money to aid those affected by the destruction. The Company and its employees donated more than $3.6 million to the Red Cross disaster relief fund – including a $1 million contribution by our founder and chairman, Pete Nicholas, and his family. We were honored to receive the American Red Cross Circle of Humanitarian Award on behalf of all our employees and their families who generously contributed their time and financial resources to help those in need.

In addition, Boston Scientific made a variety of contributions to many organizations like the American Heart Association, the Greater Boston Food Bank, the United Way and Challenged Athletes Incorporated.

A caregiver administering a diabetes test in Jamaica Plain, Massachusetts – as part of the Boston Health Care for the Homeless Program.

Students in the lab (above) and the classroom (below) at the University of Minnesota, where we've established the Boston Scientific Biomedical Engineering Fellowship Fund.

MAKING AN IMPACT ON OUR COMMUNITIES

As an extension of our mission to improve lives through medical innovation, Boston Scientific and its employees are contributing resources, time and effort to communities around the world. Here are a few examples.

Boston Health Care for the Homeless Program
This organization benefits from one of five national grants supported by the Boston Scientific Foundation through its Health Disparities Initiative, which supports innovations in patient self-management in selected community health centers that serve those who are poor, uninsured or otherwise disenfranchised. The Boston Health Care for the Homeless Program provides access to quality healthcare for homeless individuals and families in the greater Boston area.

University of Minnesota Foundation
In 2005, Boston Scientific contributed $500,000 to the University of Minnesota Foundation to fund the creation of a Boston Scientific Biomedical Engineering Fellowship Fund. The fund will help support new full-time graduate students in the Department of Biomedical Engineering – students who may someday develop medical technologies that help save or improve lives.

Family Health Centers of San Diego
Family Health Centers of San Diego provides primary healthcare, health education and secondary health services to low-income residents of San Diego County. A 2005 grant from the Boston Scientific Foundation supports the Early Life Development Screening and Parent Education Program, which provides regular screenings and health education to low-income parents of high-risk children aged three and under.

Five of the Millions of Reasons We Set Such High Standards

For Boston Scientific, the final arbiter of success is always our impact on patients. Patients are the ultimate beneficiaries of the higher standards we set: rigorous clinical science, honest information, more innovation, higher quality. Achieving the best outcomes possible for the most patients drives everything we do.

Kathleen Thompson | Kathleen suffered from coronary artery disease, which was further complicated by diabetes and insulin dependency. Instead of open-heart surgery, Kathleen and her physician opted for a less-invasive vascular intervention using Boston Scientific's TAXUS® Express²™ paclitaxel-eluting coronary stent system. Since the procedure, Kathleen – a 20-year Air Force veteran, mother of two and impassioned shopper – no longer experiences the chest pain and shortness of breath she once did.

Ron Meddings | Carotid artery disease is a condition that constricts the flow of blood and oxygen to the brain, and can lead to stroke or even death. After Ron's physician discovered blockages in his carotid arteries (previously treated by surgery), he enrolled Ron in the BEACH clinical trial. Through the trial, Ron received bilateral Carotid WALLSTENT® Monorail® Endoprosthesis stents. After a 55-minute implantation procedure, Ron was released the next day, still able to make his weekend tee time.

Nicholas Cardellechio | Nick suffered from BPH (benign prostatic hyerplasia), which can affect normal urination patterns. After several drug-based treatments failed, Nick's urologist recommended a new procedure using the Prolieve Thermodilatation® System. The procedure is minimally invasive, takes less than an hour and allows patients to go home the same day without the need for a catheter. For Nick – an attorney and paramedic instructor – this procedure allowed him to tackle his busy schedule with confidence.

Jana Gersten | After a bone injury in 2004, Jana was diagnosed with CRPS (complex regional pain syndrome), a neurological condition characterized by disabling, chronic pain. Jana's relief finally came in the form of an innovative, implantable neurostimulation device from Boston Scientific's Neuromodulation Group. Free from CRPS's debilitating pain, Jana is back to performing everyday activities that most of us take for granted, like cooking, exercising and playing with her dog, Charlie.

Michelle and Ellie Tjelmeland | Michelle and her daughter Ellie were both diagnosed profoundly deaf – Michelle due to hearing loss during her pregnancy, and Ellie at birth. Cochlear implant devices from Boston Scientific's Auditory business have benefited each of them. Michelle's restored hearing has helped her advance her career and establish the award-winning Cochlear Implant Awareness Foundation. And Ellie has learned speech, excelled in the classroom and even learned a guitar chord or two.

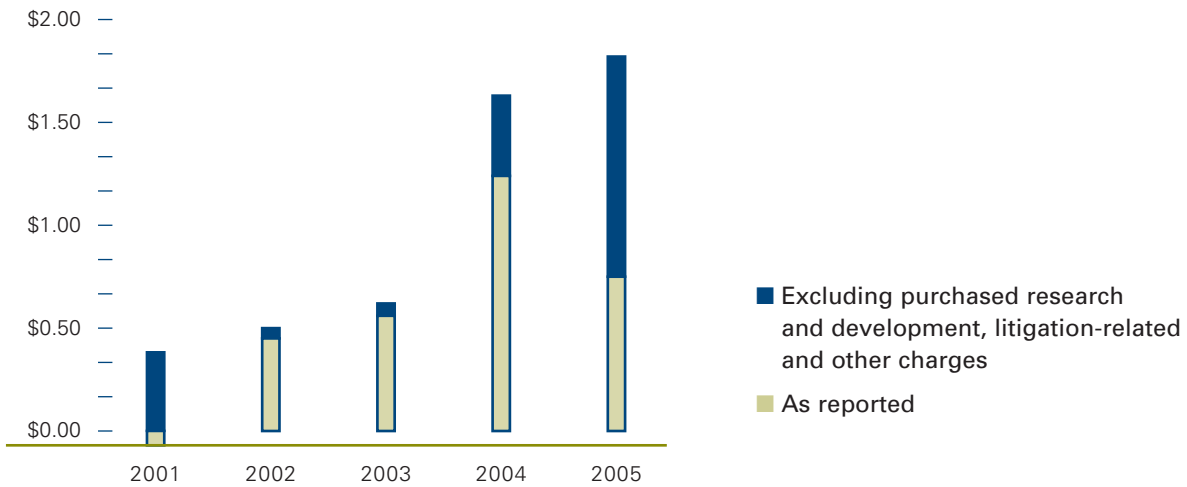
Boston Scientific Corporation Five-Year Financial Highlights

UNAUDITED

(in millions, except per share data)	2001	2002	2003	2004	2005
Net sales	$ 2,673	$ 2,919	$ 3,476	$ 5,624	$ 6,283
Net income (loss), as reported	$ (54)	$ 373	$ 472	$ 1,062	$ 628
Purchased research and development, litigation-related and other charges, net of income taxes[1]	377	40	49	332	894
Net income excluding purchased research and development, litigation-related and other charges	**$ 323**	**$ 413**	**$ 521**	**$ 1,394**	**$ 1,522**
Diluted net income (loss) per share, as reported	$ (0.07)	$ 0.45	$ 0.56	$ 1.24	$ 0.75
Purchased research and development, litigation-related and other charges per diluted share[1]	0.47	0.05	0.06	0.39	1.07
Diluted net income per share excluding purchased research and development, litigation-related and other charges	**$ 0.40**	**$ 0.50**	**$ 0.62**	**$ 1.63**	**$ 1.82**
Weighted average shares outstanding – assuming dilution	802.8	830.0	845.4	857.7	837.6

[1] see Management's Discussion and Analysis for further discussion

Diluted Net Income Per Share



We provide net income excluding certain charges and net income per share amounts excluding certain charges, in order to provide meaningful supplemental information regarding our operational performance and our prospects for the future. These supplemental measures exclude the impact of certain charges that are highly variable and difficult to predict. Management uses these supplemental measures to evaluate performance period over period, to analyze the underlying trends in our business and to establish operational goals and forecasts that are used in allocating resources. Although we believe it is useful for investors to see core performance free of special items, investors should understand that the excluded items are actual expenses that may impact the cash available for other uses. To gain a complete picture of our performance, including the effects on our net income and net income per share from special items, management does (and investors should) rely upon the GAAP income statement.

Readers are therefore reminded that non-GAAP numbers are merely a supplement to, and not a replacement for, GAAP financial measures. It should be noted as well that our non-GAAP information may be different from the non-GAAP information provided by other companies.

2005

Consolidated Financial Statements

BOSTON SCIENTIFIC AND SUBSIDIARIES

Overview

Boston Scientific Corporation is a worldwide developer, manufacturer and marketer of medical devices that are used in a broad range of interventional medical specialties including interventional cardiology, peripheral interventions, vascular surgery, electrophysiology, neurovascular intervention, oncology, endoscopy, urology, gynecology and neuromodulation. Our mission is to improve the quality of patient care and the productivity of healthcare delivery through the development and advocacy of less-invasive medical devices and procedures. This mission is accomplished through the continuing refinement of existing products and procedures and the investigation and development of new technologies that can reduce risk, trauma, cost, procedure time and the need for aftercare. Our approach to innovation combines internally developed products and technologies with those we obtain externally through our strategic acquisitions and alliances.

Our management's discussion and analysis (MD&A) begins with an executive summary that outlines our financial highlights during 2005 and focuses on the impact of drug-eluting stents to our operations. In addition, our executive summary will discuss the significance of the proposed Guidant Corporation acquisition to our future growth. Following the executive summary is an examination of the material changes in our operating results for 2005 as compared to 2004 and our operating results for 2004 as compared to 2003. The operating results are supplemented by an in-depth look at the major issues we believe are most relevant to our current and future prospects, including the proposed acquisition of Guidant. The discussion then provides an examination of liquidity, focusing primarily on material changes in our operating, investing and financing cash flows, as depicted in our statements of cash flows, and the trends underlying these changes. In addition, we will highlight the impact of the potential Guidant acquisition on our future liquidity. Finally, the MD&A provides information on our critical accounting policies.

Executive Summary

Our net sales in 2005 increased to $6,283 million from $5,624 million in 2004, an increase of 12 percent. Excluding the favorable impact of $25 million of foreign currency fluctuations, our net sales increased 11 percent. Our gross profit increased to $4,897 million, or 77.9 percent of net sales, in 2005 from $4,332 million, or 77.0 percent of net sales, in 2004. Our reported net income for 2005 was $628 million, or $0.75 per diluted share, as compared to $1,062 million, or $1.24 per diluted share, in 2004. Our reported results included net after-tax charges of $894 million, or $1.07 per diluted share, in 2005 as compared to net after-tax charges of $332 million, or $0.39 per diluted share, in 2004.[1] In addition, our cash provided by operating activities was $903 million in 2005, which includes $750 million paid for the Medinol settlement, as compared to $1,804 million in 2004.

The growth in 2005 resulted largely from a full year of sales of our TAXUS® Express²™ paclitaxel-eluting coronary stent system that we launched in the United States in March 2004 and increased sales of the TAXUS stent system in our Europe and Inter-Continental markets. TAXUS stent sales in 2005 were $2,556 million as compared $2,143 million in 2004, an increase of 19 percent. We have achieved and maintained leading drug-eluting stent market positions within our U.S., Europe and Inter-Continental markets. Further, due to increased penetration rates and the successful launch of our next-generation TAXUS® Liberté™ paclitaxel-eluting coronary stent system in our Europe and Inter-Continental markets, our international TAXUS stent system sales for 2005 increased by 38 percent as compared to 2004. This increase in sales was offset by decreased TAXUS stent system sales in the U.S. during the second half of 2005, as compared to the same period in the prior year largely due to a reduction in market share, as well as pricing pressure. During the first three quarters of 2005, we experienced sequential declines in our market share. In the fourth quarter of 2005, our market share stabilized and was relatively consistent with the prior quarter. We expect to launch our TAXUS Liberté stent system in the U.S. in the second half of 2006 and our TAXUS Express² stent system in Japan in the first half of 2007, subject to regulatory approvals.

In addition, during 2005, our worldwide Endosurgery group sales increased to $1,228 million from $1,088 million in 2004, an increase of 13 percent. Further, our Neuromodulation division, formed following the June 2004 acquisition of Advanced Bionics Corporation, generated $148 million in net sales during 2005 as compared to $46 million in 2004, which represents the period following the acquisition.

[1] The 2005 net after-tax charges consisted of a $598 million litigation settlement with Medinol Ltd.; $267 million in purchased research and development primarily attributable to our recent acquisitions; $24 million of asset write-downs and employee-related costs that resulted from certain business optimization initiatives; $11 million in expenses related to certain retirement benefits; and a $6 million tax adjustment associated with a technical correction made to the American Jobs Creation Act. The 2004 net after-tax charges consisted of a $75 million provision for legal and regulatory exposures; a $71 million enhancement to our 401(k) Retirement Savings Plan; $65 million of purchased research and development; a $61 million charge relating to taxes on the approximately $1 billion of cash that we repatriated in 2005 under the American Jobs Creation Act of 2004; and a $60 million non-cash charge resulting from certain modifications to our stock option plans.

During 2005, we invested a portion of our increased gross profit in various research and development initiatives, particularly related to our 2004 acquisition of Advanced Bionics and our 2005 acquisition of TriVascular, Inc., as well as on projects within our Endosurgery group, including our Endovations™ Endoscopy Suite. We funded additional headcount and programs to strengthen our sales and marketing organization and we made enhancements to our manufacturing and distribution network.

We continued to generate strong operating cash flow during 2005. In addition, due to favorable market conditions, we raised $750 million from the public markets through a November 2005 debt offering. We used cash generated from operating activities and from the public debt issuance to: repay short-term debt obligations; repurchase shares of our common stock on the open market; and fund 2005 strategic alliances and acquisitions.

Recent Developments

On January 25, 2006, we entered into a definitive agreement to acquire Guidant Corporation for an aggregate purchase price of $27 billion (net of proceeds from option exercises), which represents a combination of cash and stock worth $80 per share of Guidant common stock. We expect that this acquisition will enable us to become a major provider in the high-growth cardiac rhythm management business, significantly diversifying our revenue stream across multiple business segments and enhancing our overall competitive position. In addition, in conjunction with the acquisition of Guidant, Abbott Laboratories has agreed to acquire Guidant's vascular intervention and endovascular businesses and has agreed to share the drug-eluting stent technology it acquires from Guidant with us. This will enable us to access a second drug-eluting stent program that will complement our existing TAXUS stent program. The transaction is subject to customary closing conditions, including clearances under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 and the European Union merger control regulation, as well as approval of Boston Scientific and Guidant shareholders. Subject to these conditions, we currently expect the acquisition to occur during the week of April 3, 2006.

On January 26, 2006, we received a corporate warning letter from the FDA notifying us of serious regulatory problems at three facilities and advising us that our corporate wide corrective action plan relating to three warning letters issued to us in 2005 was inadequate. As also stated in this FDA warning letter, the FDA will not grant our requests for exportation certificates to foreign governments or approve pre-market approval applications for our class III devices to which the quality control or current good manufacturing practices deficiencies described in the letter are reasonably related until the deficiencies described in the letter have been corrected. We intend to resolve the quality issues cited by the FDA prior to the anticipated launch of our TAXUS Liberté stent system in the United States and therefore do not anticipate delays of this product. However, while we believe we can remediate these issues in an expeditious manner, there can be no assurances regarding the length of time it will take to resolve these issues to the satisfaction of the FDA, and any such resolution may require the dedication of significant incremental internal and external resources. In addition, if our remedial actions are not satisfactory to the FDA, the FDA may take further regulatory actions against us, including but not limited to seizing our product inventory, obtaining a court injunction against further marketing of our products or assessing civil monetary penalties.

Results of Operations

Net Sales

The following table provides our net sales by region and the relative change on an as reported and constant currency basis:

				2005 versus 2004		2004 versus 2003	
(in millions)	2005	2004	2003	As Reported Currency Basis	Constant Currency Basis	As Reported Currency Basis	Constant Currency Basis
United States	**$3,852**	**$3,502**	**$1,924**	**10%**	**10%**	**82%**	**82%**
Europe	$1,161	$ 994	$ 672	17%	17%	48%	35%
Japan	579	613	541	(6)%	(4)%	13%	6%
Inter-Continental	691	515	339	34%	28%	52%	44%
International	**$2,431**	**$2,122**	**$1,552**	**15%**	**13%**	**37%**	**27%**
Worldwide	**$6,283**	**$5,624**	**$3,476**	**12%**	**11%**	**62%**	**57%**

The following table provides our worldwide net sales by division and the relative change on an as reported and constant currency basis:

				2005 versus 2004		2004 versus 2003	
(in millions)	2005	2004	2003	As Reported Currency Basis	Constant Currency Basis	As Reported Currency Basis	Constant Currency Basis
Cardiovascular	$4,498	$4,107	$2,168	10%	9%	89%	84%
Electrophysiology	132	130	113	2%	2%	15%	12%
Neurovascular	277	253	223	9%	9%	13%	9%
Cardiovascular	**$4,907**	**$4,490**	**$2,504**	**9%**	**9%**	**79%**	**74%**
Oncology	$ 207	$ 186	$ 166	11%	11%	12%	8%
Endoscopy	697	641	580	9%	9%	11%	7%
Urology/ Gynecology	324	261	226	24%	24%	15%	13%
Endosurgery	**$1,228**	**$1,088**	**$ 972**	**13%**	**13%**	**12%**	**9%**
Neuromodulation	**$ 148**	**$ 46**	**N/A**	**222%**	**222%**	**N/A**	**N/A**
Worldwide	**$6,283**	**$5,624**	**$3,476**	**12%**	**11%**	**62%**	**57%**

We manage our international operating regions and divisions on a constant currency basis, while market risk from currency exchange rate changes is managed at the corporate level.

U.S. Net Sales

In 2005, our U.S. net sales increased by $350 million, or 10 percent, as compared to 2004. The increase primarily related to $1,763 million in sales of our TAXUS stent system for 2005 as compared to $1,570 million for 2004. We launched our TAXUS stent system in the U.S. late in the first quarter of 2004 and estimate that physicians in the U.S. have converted approximately 88 percent of the stents they use in interventional procedures from bare-metal stents to drug-eluting stents as of December 31, 2005, as compared to 85 percent at December 31, 2004. The remainder of the increase in our U.S. net sales related to sales growth of $83 million from our Endosurgery group and $75 million from our Neuromodulation division. This increase in sales was offset by decreased TAXUS stent system sales in the U.S. during the second half of 2005, as compared to the same period in the prior year largely due to a reduction in market share, as well as pricing pressure. During the first three quarters of 2005, we experienced sequential declines in our market share. In the fourth quarter of 2005, our market share stabilized and was relatively consistent with the prior quarter.

In 2004, our U.S. net sales increased by $1,578 million, or 82 percent, as compared to 2003. The increase related primarily to $1,570 million in sales of our TAXUS stent system. Declines in our bare-metal stent revenue by $155 million to $59 million in 2004 partially offset this increase, as physicians continued to convert the stents they use in interventional procedures from bare-metal stents to drug-eluting stents, including our TAXUS stent system. Sales from other products within our Cardiovascular division also increased by $49 million, or five percent, during 2004. The remainder of the increase in our U.S. revenues related to sales growth in each of our other U.S. divisions, including $37 million in sales from our Neuromodulation division.

International Net Sales

In 2005, our international net sales increased by $309 million, or 15 percent, as compared to 2004. The increase related primarily to sales growth of our TAXUS stent system by $220 million, or 38 percent, in our Europe and Inter-Continental markets. As of December 31, 2005, we estimate that physicians in our Europe and Inter-Continental markets have converted approximately 49 percent of the stents they use in interventional procedures from bare-metal stents to drug-eluting stents, as compared to approximately 40 percent at the end of 2004. Conversion rates have been more gradual in these markets than in the U.S. primarily due to the timing of local reimbursement and funding levels. In addition, we successfully launched our TAXUS Liberté stent system in certain Inter-Continental markets during the first quarter of 2005 and in Europe during the third quarter of 2005. The remainder of the increase in our revenue in these markets was due to growth in various product franchises, including $57 million in incremental sales from our Endosurgery group, and $27 million in sales growth from our Neuromodulation division.

In 2005, our Japan net sales decreased by $34 million, or six percent, as compared to 2004 primarily due to decreased sales from our Cardiovascular division. We have experienced declining coronary stent sales in Japan since a competitor launched its drug-eluting stent in this market late in the second quarter of 2004. Due to the timing of regulatory approval for our TAXUS stent system and government-mandated pricing reductions for other products, we do not expect revenue growth in our existing Japan business until we receive regulatory approval and launch our drug-eluting stent in Japan, which we expect to occur in the first half of 2007.

In 2004, our international net sales increased by $570 million, or 37 percent, as compared to 2003. Excluding the favorable impact of $155 million of foreign currency fluctuations, international net sales increased 27 percent. The increase related primarily to sales growth of our TAXUS stent system by $375 million, or 189 percent, in our Europe and Inter-Continental markets. We launched the TAXUS stent system in these markets during the first quarter of 2003. In addition, in 2004 our Japan net sales increased by $72 million, or 13 percent, as compared to 2003 primarily due to sales of our Express^2 stent system, which we launched in Japan during the first quarter of 2004. The remainder of the increase in our revenue in these markets was due to incremental growth in various product franchises, none of which were individually significant.

Gross Profit

The following table provides a summary of our gross profit:

	2005		2004		2003	
(in millions)	$	% of Net Sales	$	% of Net Sales	$	% of Net Sales
Gross profit	4,897	77.9	4,332	77.0	2,515	72.4

In 2005, our gross profit, as a percentage of net sales, increased by 0.9 percentage points as compared to 2004. Shifts in our product sales mix toward higher margin products, primarily drug-eluting coronary stent systems, increased our gross profit as a percentage of net sales by 0.6 percentage points. Our gross

profit percentage increased by 1.0 percentage point related to $57 million in inventory write-downs in 2004, including a $43 million write-down attributable to our recalls of certain coronary stent systems and a $14 million write-down of TAXUS stent inventory due to shelf-life dating. Our gross profit for 2005 was reduced as a percentage of net sales by 0.9 percentage points related to period expenses, including manufacturing start-up costs primarily associated with our TAXUS Liberté stent system and increased investment in quality initiatives. The remaining fluctuation in gross profit as a percentage of net sales primarily related to the favorable impact of changes in foreign exchange rates.

In 2004, our gross profit, as a percentage of net sales, increased by 4.6 percentage points as compared to 2003. Shifts in our product sales mix toward higher margin products, primarily drug-eluting coronary stent systems in the U.S., increased our gross profit as a percentage of net sales by 6.5 percentage points. This improvement in our gross profit as a percentage of net sales was partially reduced by 1.0 percentage point related to $57 million in inventory write-downs. In addition, other expenses primarily associated with increased investments in our manufacturing capabilities reduced gross profit as a percentage of net sales during 2004 by approximately 1.0 percentage point.

Operating Expenses

The following table provides a summary of certain of our operating expenses:

	2005		2004		2003	
(in millions)	$	% of Net Sales	$	% of Net Sales	$	% of Net Sales
Selling, general and administrative expenses	1,814	28.9	1,742	31.0	1,171	33.7
Research and development expenses	680	10.8	569	10.1	452	13.0
Royalty expense	227	3.6	195	3.5	54	1.6
Amortization expense	152	2.4	112	2.0	89	2.6

Selling, General and Administrative (SG&A) Expenses

In 2005, our SG&A expenses increased by $72 million, or four percent, as compared to 2004. The increase primarily related to: approximately $100 million in increased headcount and higher compensation expense mainly attributable to the expansion of the sales force within our Interventional Cardiology business unit and Endosurgery group and costs related to market development initiatives; $75 million in incremental operating expenses associated with our 2004 and 2005 acquisitions, primarily Advanced Bionics; $21 million in employee-related costs primarily attributable to optimization initiatives within our human resources function and international divisions; $19 million in stock compensation expense primarily associated with the issuance of deferred stock units in 2005; and $17 million in costs related to certain retirement benefits. Certain charges incurred in 2004 partially offset these increases, including a $110 million enhancement to our 401(k) Plan, and a $90 million non-cash charge resulting from certain modifications to our stock option plans. As a percentage of our net sales, SG&A expenses decreased to 28.9 percent in 2005 from 31.0 percent in 2004 primarily due to the increase in our net sales in 2005.

In 2004, our SG&A expenses increased by $571 million, or 49 percent, as compared to 2003. The increase primarily related to: approximately $200 million in additional marketing programs, increased headcount and higher sales force commission expenses, mainly attributable to our TAXUS stent program and, to a lesser degree, to support our other product franchises; and approximately $40 million due to the impact of foreign currency fluctuations. In addition, our SG&A expenses in 2004 included charges of $110 million attributable to an enhancement to our 401(k) Plan and $90 million resulting from certain modifications to our stock option plans. Further, our SG&A expenses included $40 million in operating expenses associated with our acquisition of Advanced Bionics. As a percentage of our net sales, SG&A expenses decreased to 31.0 percent in 2004 from 33.7 percent in 2003 primarily due to the significant increase in our net sales in 2004.

Research and Development Expenses

Our investment in research and development reflects spending on regulatory compliance and clinical research as well as new product development programs. In 2005, our research and development expenses increased by $111 million, or 20 percent, as compared to 2004. As a percentage of our net sales, research and development expenses increased to 10.8 percent in 2005 from 10.1 percent in 2004. The increase primarily related to approximately $60 million in incremental research and development expenses attributable to our 2004 and 2005 acquisitions, primarily Advanced Bionics and TriVascular. In addition, we increased spending on internal research and development projects within our Endosurgery group by $25 million, including increased spending on our Endovations Endoscopy Suite.

In 2004, our research and development expenses increased by $117 million, or 26 percent, as compared to 2003. The increase related primarily to an increased investment of approximately $50 million in our Cardiovascular division, which was mainly associated with our next-generation stent platforms. In addition, our research and development expenses in 2004 included $25 million attributable to our acquisition of Advanced Bionics.

The remainder of the growth in our research and development spending reflects investments to enhance our clinical and regulatory infrastructure and provide additional funding for research and development on next-generation and novel technology offerings across multiple programs and divisions. As a percentage of our net sales, research and development expenses decreased to 10.1 percent in 2004 from 13.0 percent in 2003 primarily due to the significant increase in our net sales in 2004.

Royalty Expense

In 2005, our royalty expense increased by $32 million, or 16 percent, as compared to 2004. As a percentage of net sales, royalty expense increased to 3.6 percent in 2005 from 3.5 percent in 2004. The increase in our royalty expense related to sales growth of royalty-bearing products, primarily sales of our TAXUS stent system. Royalty expense attributable to sales of our TAXUS stent system increased by $27 million to $174 million for 2005 as compared to 2004.

In 2004, our royalty expense increased by $141 million, or 261 percent, as compared to 2003. As a percentage of net sales, royalty expense increased to 3.5 percent in 2004 from 1.6 percent in 2003. The increase in our royalty expense related to sales growth of royalty-bearing products, primarily sales of our TAXUS stent system. Royalty expense attributable to sales of our TAXUS stent system increased by $137 million to $147 million for 2004 as compared to 2003. In November 2004, we exercised our right under an existing licensing agreement with Angiotech Pharmaceuticals, Inc. to obtain an exclusive license for the use of paclitaxel and other agents for certain applications in the coronary vascular field.

Amortization Expense

In 2005, our amortization expense increased by $40 million, or 36 percent, as compared to 2004. As a percentage of our net sales, amortization expense increased to 2.4 percent in 2005 from 2.0 percent in 2004. The increase in our amortization expense was primarily due to $25 million in incremental amortization expense from the intangible assets obtained in conjunction with our 2004 and 2005 acquisitions, primarily Advanced Bionics. In addition, our amortization expense included a $10 million write-off of intangible assets related to our Enteryx® Liquid Polymer Technology (Enteryx), a discontinued technology platform obtained as a part of our acquisition of Enteric Medical Technologies, Inc. The write-off resulted from our decision during the third quarter of 2005 to cease selling the Enteryx product.

In 2004, our amortization expense increased by $23 million, or 26 percent, as compared to 2003. The increase related primarily to the amortization of intangible assets from our acquisitions in 2004 of Advanced Bionics and Precision Vascular Systems, Inc. (PVS). Amortization expense for these two acquisitions was $17 million in 2004. As a percentage of our net sales, amortization expense decreased to 2.0 percent in 2004 from 2.6 percent in 2003 primarily due to the significant increase in our net sales in 2004.

Interest Expense and Other, Net

Our interest expense increased to $90 million in 2005 from $64 million in 2004 and $46 million in 2003. The increase in 2005 as compared to 2004 related primarily to an increase in average market interest rates on our borrowings. The increase in 2004 as compared to 2003 related primarily to an increase in our average debt levels and in average market rates on our floating-rate borrowings.

Our other, net reflected income of $13 million in 2005, expense of $16 million in 2004, and expense of $8 million in 2003. Our other, net included asset write-downs of $17 million in 2005 and $58 million in 2004 associated with certain investments in and loans to privately held and publicly traded companies. We do not believe that these write-downs of assets will have a material impact on our future operations. In 2004, our other, net included realized gains of $36 million from sales of investments in privately held and publicly traded companies. In addition, our other, net included interest income of $36 million in 2005, $20 million in 2004, and $6 million in 2003. Our interest income increased in 2005 as compared to 2004 due to increases in average market interest rates. Our interest income in 2004 increased as compared to 2003 due primarily to growth in our cash balances.

Tax Rate

The following table provides a summary of our reported tax rate:

				Percentage Point Increase	
	2005	2004	2003	2005 versus 2004	2004 versus 2003
Reported tax rate	29.5%	28.9%	26.6%	0.6	2.3
Impact of certain charges	5.5%	4.9%	1.6%	0.6	3.3

In 2005, the increase in our reported tax rate as compared to 2004 related primarily to the impact of certain charges during 2005 that are taxed at different rates than our effective tax rate. These charges include: certain litigation-related charges; purchased research and development; asset write-downs and employee-related costs that resulted from certain business optimization initiatives; costs related to certain retirement benefits;

and a tax adjustment associated with a technical correction made to the American Jobs Creation Act.

Management currently estimates that our 2006 effective tax rate, excluding certain charges, will be approximately 23 percent primarily due to our intention to reinvest substantially all of our offshore earnings. However, geographic changes in the manufacture of our products may positively or negatively impact our effective tax rate.

In 2004, the increase in our reported tax rate as compared to 2003 related primarily to the net impact of certain charges during 2004 that were taxed at different rates than our effective tax rate. These charges included: a provision for an extraordinary dividend related to overseas cash balances we repatriated in 2005 pursuant to the American Jobs Creation Act; an accrual for our legal and regulatory exposures; an enhancement to our 401(k) Plan; purchased research and development; and a non-cash charge resulting from certain modifications to our stock option plans. In addition, our effective tax rate was favorably impacted by more revenue being generated from products manufactured in lower tax jurisdictions.

Litigation-Related Charges and Credits

In 2005, we recorded a $780 million pre-tax charge associated with the Medinol litigation settlement. On September 21, 2005, we reached a settlement with Medinol resolving certain contract and patent infringement litigation. In conjunction with the settlement agreement, we paid $750 million in cash and cancelled our equity investment in Medinol.

In 2004, we recorded a $75 million provision for certain legal and regulatory matters, which included the civil settlement with the U.S. Department of Justice, which was paid in the second quarter of 2005.

In 2003, we agreed to settle a number of our outstanding product liability cases. The cost of settlement in excess of our available insurance limits was $8 million. In addition, during 2003, we recorded a $7 million charge related to an adverse judgment in a suit filed by the Federal Trade Commission.

Purchased Research and Development

In 2005, we recorded $276 million of purchased research and development. Our 2005 purchased research and development consisted of: $130 million relating to our acquisition of TriVascular; $73 million relating to our acquisition of Advanced Stent Technologies, Inc. (AST); $45 million relating to our acquisition of Rubicon Medical Corporation; and $3 million relating to our acquisition of CryoVascular Systems, Inc. In addition, we recorded $25 million of purchased research and development in conjunction with obtaining distribution rights for new brain monitoring technology that Aspect Medical Systems, one of our strategic partners, is currently developing. This technology is designed to aid the diagnosis and treatment of depression, Alzheimer's disease and other neurological conditions.

The most significant 2005 purchased research and development projects included TriVascular's abdominal aortic aneurysms (AAA) stent-graft and AST's Petal™ bifurcation stent, which collectively represented 73 percent of our 2005 purchased research and development. TriVascular's AAA stent-graft design reduces the size of the stent-graft by replacing much of the metal stent assembly with a polymer that is injected into channels within the stent-graft during the procedure. During the fourth quarter of 2005, management decided to re-design certain aspects of the stent-graft to enhance patient safety and to improve product performance. The re-design will result in incremental costs and time to complete the project relative to those expected at the date of acquisition. We currently expect to launch the AAA stent-graft in the U.S. by 2011 and to incur approximately $200 million of research and development costs over the next five years to complete the project. We continue to assess the pace of development and our opportunities within this market, which may result in a delay in the timing of regulatory approval.

AST's Petal bifurcation stent is designed to expand into the side vessel when a single vessel branches into two vessels, permitting blood to flow into both branches of the bifurcation and providing support at the junction. We estimate the cost to complete the Petal bifurcation stent to be between $100 million and $125 million. As of the date we acquired AST, we expected the Petal bifurcation stent to be commercially available on a worldwide basis within six years in a drug-eluting configuration.

In 2004, we recorded $65 million of purchased research and development. Our 2004 purchased research and development consisted primarily of $50 million relating to our acquisition of Advanced Bionics and $14 million relating to our acquisition of PVS. The most significant in-process projects acquired in connection with our 2004 acquisitions included Advanced Bionics' bion® microstimulator and drug delivery pump, which collectively represented 77 percent of our 2004 acquired in-process projects' value. The bion microstimulator is an implantable neurostimulation device designed to treat a variety of neurological conditions, including migraine headaches and urge incontinence. The cost to complete the bion microstimulator is estimated to be between $35 million and $45 million. We expect that the bion microstimulator will be commercially available within three years.

The Advanced Bionics drug delivery pump is an implanted programmable device designed to treat chronic pain. The cost to complete the drug delivery pump is estimated to be between $30 million and $40 million. We continue to assess the pace of development and our opportunities for the drug delivery pump, which may result in a delay in the timing of regulatory approval.

In 2003, we recorded $37 million of purchased research and development. Our 2003 purchased research and development consisted of $9 million relating to our acquisition of InFlow Dynamics, Inc. and $28 million relating primarily to certain acquisitions we consummated in prior years. The in-process projects acquired in connection with our acquisition of InFlow were not significant to our consolidated results. The purchased research and development associated with the prior years' acquisitions related primarily to our 2001 acquisition of Embolic Protection, Inc. and resulted from consideration that was contingent at the date of acquisition, but earned during 2003.

In connection with our 2002 acquisitions, we acquired several in-process projects, including Smart Therapeutics, Inc.'s atherosclerosis stent. The atherosclerosis stent is a self-expanding nitinol stent designed to treat narrowing of the arteries around the brain. During 2005, we completed the atherosclerosis stent in-process project and received Humanitarian Device Exemption approval to begin selling this technology on a limited basis. The total cost for us to complete the project was approximately $10 million.

In connection with our 2001 acquisitions, we acquired several significant in-process projects, including Interventional Technologies, Inc.'s next-generation Cutting Balloon® device. The Cutting Balloon device is a novel balloon angioplasty device with mounted scalpels that relieve stress in the artery, reducing the force necessary to expand the vessel. During 2005, we completed the Cutting Balloon in-process project and received FDA approval for this technology. The total cost for us to complete the project was approximately $7 million.

Outlook

Coronary Stents

Coronary stent revenue represented 43 percent of our consolidated net sales during 2005, and approximated $2,693 million in 2005 as compared to $2,351 million in 2004. We estimate that the worldwide coronary stent market will approximate $6 billion in 2006, as compared to $5.9 billion in 2005. Drug-eluting stents are estimated to represent approximately 87 percent of the dollar value of the worldwide coronary stent market in 2005 and 90 percent in 2006. As of the fourth quarter of 2005, we believe that the U.S. stent market has been substantially penetrated and estimate that physicians in the U.S. have converted approximately 88 percent of the stents they use in interventional procedures from bare-metal stents to drug-eluting stents. We have experienced declines in our U.S. drug-eluting stent revenues in the second half of 2005 as compared to the same period in the prior year largely as a result of a reduction in market share, as well as pricing pressure. During the first three quarters of 2005, we experienced sequential declines in our market share. In the fourth quarter of 2005, our market share stabilized and was relatively consistent with the prior quarter. We expect to launch our TAXUS Liberté stent system in the U.S. during the second half of 2006, subject to regulatory approval.

As of the fourth quarter of 2005, we estimate that physicians in our Europe and Inter-Continental markets have converted approximately 49 percent of the stents they use in interventional procedures from bare-metal stents to drug-eluting stents, as compared to approximately 40 percent at the end of 2004. We expect that conversion rates will continue to increase in our Europe and Inter-Continental markets. We successfully launched our TAXUS Liberté stent system in certain Inter-Continental markets during the first quarter of 2005 and in Europe during the third quarter of 2005. We believe our TAXUS Liberté stent system represents a driver of future revenue in these markets. Further, we expect to launch our TAXUS Express^2 stent system in Japan during the first half of 2007, subject to regulatory approval, where we estimate the size of the market in 2007 to approximate $700 million.

Historically, the worldwide coronary stent market has been dynamic and highly competitive with significant market share volatility. In addition, in the ordinary course of our business, we conduct and participate in numerous clinical trials with a variety of study designs, patient populations and trial endpoints. Unfavorable or inconsistent clinical data from existing or future clinical trials conducted by us, by our competitors or by third parties, or the market's perception of this clinical data, may adversely impact our position in and share of the drug-eluting stent market and may contribute to increased volatility in the market.

We believe that we can maintain a leadership position within the drug-eluting stent markets in which we compete for a variety of reasons, including:

- the positive and consistent results of our TAXUS clinical trials;
- the performance benefits of our current technology;

- the strength of our pipeline of drug-eluting stent products and the planned launch sequence of these products;
- our overall market leadership in interventional medicine and our sizeable interventional cardiology sales force; and
- our significant investments in our sales, clinical, marketing and manufacturing capabilities.

A material decline in our drug-eluting stent revenue would have a significant adverse impact on our future operating results. The most significant variables that may impact the size of the drug-eluting coronary stent market and our position within this market include:

- entry of additional competitors in international markets and the U.S.;
- declines in the average selling prices of drug-eluting stent systems;
- variations in clinical results or product performance of our and our competitions' products;
- new competitive product launches;
- delayed or limited regulatory approvals and reimbursement policies;
- litigation related to intellectual property;
- continued physician confidence in our technology;
- the average number of stents used per procedure;
- expansion of indications for use;
- a reduction in the overall number of procedures performed;
- the international adoption rate of drug-eluting stent technology; and
- the level of supply of our drug-eluting stent system and competitive stent systems.

Our drug-eluting stent system is currently one of only two drug-eluting products in the U.S. market. Our share of the drug-eluting stent market, as well as unit prices, are expected to continue to be adversely impacted as additional significant competitors enter the drug-eluting stent market, which began during the third quarter of 2005 internationally and is expected to occur during the second half of 2007 in the U.S.

The manufacture of our TAXUS stent system involves the integration of multiple technologies, critical components, raw materials and complex processes. Significant favorable or unfavorable changes in forecasted demand as well as disruptions associated with our TAXUS stent manufacturing process may impact our inventory levels. Variability in expected demand or the timing of the launch of next-generation products may result in excess or expired inventory positions and future inventory charges.

Regulatory Compliance

The trend in countries around the world, including the U.S. and Japan, toward more stringent regulatory requirements for product clearance, changing reimbursement models and more rigorous inspection and enforcement activities has generally caused or may cause medical device manufacturers like us to experience more uncertainty, delay, risk and expense. On January 26, 2006, we received a corporate warning letter from the FDA notifying us of serious regulatory problems at three facilities and advising us that our corporate wide corrective action plan relating to three warning letters issued to us in 2005 was inadequate. As also stated in this FDA warning letter, the FDA will not grant our requests for exportation certificates to foreign governments or approve pre-market approval applications for our class III devices to which the quality control or current good manufacturing practices deficiencies described in the letter are reasonably related until the deficiencies described in the letter have been corrected. We intend to resolve the quality issues cited by the FDA prior to the anticipated launch of our TAXUS Liberté stent system in the United States and therefore do not anticipate delays of this product. However, while we believe we can remediate these issues in an expeditious manner, there can be no assurances regarding the length of time it will take to resolve these issues to the satisfaction of the FDA, and any such resolution will likely require the dedication of significant incremental internal and external resources. In addition, if our remedial actions are not satisfactory to the FDA, the FDA may take further regulatory actions against us, including but not limited to seizing our product inventory, obtaining a court injunction against further marketing of our products or assessing civil monetary penalties.

Intellectual Property Litigation

There continues to be significant intellectual property litigation in the coronary stent market and medical device industry. We are currently involved in a number of legal proceedings with our competitors, including Johnson & Johnson and Medtronic, Inc. There can be no assurance that an adverse outcome in one or more of these proceedings would not impact our ability to meet our objectives in the market. See *Note J—Commitments and Contingencies* to our 2005 consolidated financial statements included in this Annual Report for a description of these legal proceedings.

Innovation

Our approach to innovation combines internally developed products and technologies with those we obtain externally through our strategic acquisitions and alliances. Our research and development program is largely focused on the development of next-generation and novel technology offerings across multiple programs and divisions. We expect to continue to invest aggressively in our drug-eluting stent program to achieve sustained worldwide market leadership positions. We successfully launched our TAXUS Liberté stent system in certain Inter-Continental markets during the first quarter of 2005 and in Europe during the third quarter of 2005. We expect to launch our TAXUS Liberté stent system in the U.S. during the second half of 2006, subject to regulatory approval. Further, we anticipate continuing our increased focus and spending on areas outside of drug-eluting stent technology. We believe our focus will be primarily on technologies in which we have already made significant investments, including neuromodulation, endoscopic systems, carotid stenting, and bifurcation stenting, but may also extend into other medical device opportunities. However, given their early stage of development, there can be no assurance that these technologies will achieve technological feasibility, obtain regulatory approval or gain market acceptance. A delay in the development or approval of these technologies or our decision to reduce funding of these projects may adversely impact the contribution of these technologies to our future growth.

Our acquisitions and alliances are intended to expand further our ability to offer our customers effective, quality medical devices that satisfy their interventional needs. Management believes it has developed a sound plan to integrate acquired businesses. However, our failure to integrate these businesses successfully could impair our ability to realize the strategic and financial objectives of these transactions. Potential future acquisitions, including companies with whom we currently have strategic alliances or options to purchase, may be dilutive to our earnings and may require additional financing, depending on their size and nature. Further, in connection with these acquisitions and other strategic alliances, we have acquired numerous in-process research and development projects. As we continue to undertake strategic initiatives, it is reasonable to assume that we will acquire additional in-process research and development projects.

In addition, we have entered a significant number of strategic alliances with privately held and publicly traded companies. Many of these alliances involve equity investments and often give us the option to acquire the other company or assets of the other company in the future. We enter these strategic alliances to broaden our product technology portfolio and to strengthen and expand our reach into existing and new markets. The success of these alliances is an important element of our growth strategy and we will continue to seek market opportunities and growth through investments in selective strategic alliances and acquisitions. However, the full benefit of these alliances is often dependent on the strength of the other companies' underlying technology and ability to execute. An inability to achieve regulatory approvals and launch competitive product offerings, or litigation related to these technologies, among other factors, may prevent us from realizing the benefit of these alliances.

Our agreement to distribute certain guidewire and sheath products will expire during the first quarter of 2006. Management has identified some replacements for these products. The sales level associated with the replacement products is expected to be less than that of our previously distributed products.

International Markets

International markets are also being affected by economic pressure to contain reimbursement levels and healthcare costs. Our profitability from our international operations may be limited by risks and uncertainties related to economic conditions in these regions, foreign currency fluctuations, regulatory and reimbursement approvals, competitive offerings, infrastructure development, rights to intellectual property and our ability to implement our overall business strategy. Any significant changes in the competitive, political, regulatory, reimbursement or economic environment where we conduct international operations may have a material impact on our business, financial condition or results of operations.

In addition, we are required to renew regulatory approvals in certain international jurisdictions, which may require additional testing and documentation. If sufficient resources are not available to renew these approvals or these approvals are not timely renewed, our ability to market our full line of existing products within these jurisdictions may be limited.

Guidant Acquisition

On January 25, 2006, we entered into a definitive agreement to acquire Guidant Corporation for an aggregate purchase price of $27 billion (net of proceeds from option exercises), which represents a combination of cash and stock worth $80 per share of Guidant common stock. We expect that this acquisition will enable us to become a major provider in the high-growth cardiac rhythm management business, significantly diversifying our revenue stream across multiple business segments and

enhancing our overall competitive position. In addition, in conjunction with the acquisition of Guidant, Abbott Laboratories has agreed to acquire Guidant's vascular intervention and endovascular businesses and has agreed to share the drug-eluting stent technology it acquires from Guidant with us. This will enable us to access a second drug-eluting stent program that will complement our existing TAXUS coronary stent program. The transaction is subject to customary closing conditions, including clearances under the Hart-Scott-Rodino Antitrust Improvements Act and the European Union merger control regulation, as well as approval of Boston Scientific and Guidant shareholders. Subject to these conditions, we currently expect the acquisition to occur during the week of April 3, 2006.

In connection with the acquisition, Boston Scientific will issue to Guidant shareholders and Abbott shares of Boston Scientific common stock. As a result of the issuance of these shares, current Boston Scientific stockholders will own a smaller percentage of Boston Scientific after the acquisition. We expect our weighted average shares outstanding, assuming dilution, to increase from approximately 840 million for 2005 to approximately 1.4 billion following the acquisition. The acquisition will also result in significant dilution to our 2006 earnings per share.

The integration of Guidant's operations and product lines with Boston Scientific will be complex and time-consuming, and the separation of the Guidant businesses required by the Abbott transaction will add complexity to the transition process. The failure to integrate Boston Scientific and Guidant successfully and to manage the challenges presented by the transition process successfully, including the retention of key Guidant personnel, may result in the combined company and its stockholders not achieving the anticipated potential benefits of the acquisition.

In addition, the combined company will incur integration and restructuring costs following the completion of the acquisition as Boston Scientific integrates certain operations of Guidant. Although Boston Scientific and Guidant expect that the realization of efficiencies related to the integration of the businesses may offset incremental transaction, merger-related and restructuring costs over time, no assurances can be made that this net benefit will be achieved in the near term, or at all.

Completion of the acquisition is conditioned upon the receipt of certain governmental authorizations, consents, orders and approvals, including the expiration or termination of the applicable waiting period, and any extension of the waiting period, under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, and approval under the European Union merger control regulation. These consents, orders and approvals may impose conditions on, or require divestitures relating to, the divisions, operations or assets of Boston Scientific or Guidant, in addition to the purchase by Abbott of Guidant's vascular and endovascular businesses, and could require modification to the terms of the Abbott transaction agreement in a manner adverse to Boston Scientific or the combined company. These conditions or divestitures may jeopardize or delay completion of the Abbott transaction or the acquisition or may reduce the anticipated benefits of the Abbott transaction or the acquisition. Further, no assurance can be given that the required consents and approvals will be obtained or that the required conditions to closing will be satisfied, and, if all required consents and approvals are obtained and the conditions are satisfied, no assurance can be given as to the terms, conditions and timing of the approvals or that they will satisfy the terms of the merger agreement. Additionally, completion of the acquisition is conditioned on the absence of certain restraining orders or injunctions by judgment, court order or law that would restrain or prohibit consummation of the acquisition. Boston Scientific and Guidant have received recent claims related to the acquisition from plaintiffs seeking an injunction to prohibit consummation of the acquisition and other relief, including monetary damages.

Liquidity and Capital Resources

The following table provides a summary of key performance indicators that we use to assess our liquidity and operating performance:

(in millions)	2005	2004	2003
Cash and cash equivalents	$ 689	$1,296	$671
Short-term marketable securities	159	344	81
Cash provided by operating activities	903	1,804	787
Cash used for investing activities	551	1,622	871
Cash (used for) provided by financing activities	(954)	439	487
EBITDA*	1,259	1,813	879

* The following represents a reconciliation between EBITDA and net income:

(in millions)	2005	2004	2003
Net income	$ 628	$1,062	$472
Income taxes	263	432	171
Interest expense	90	64	46
Interest income	(36)	(20)	(6)
Depreciation and amortization	314	275	196
EBITDA	**$1,259**	**$1,813**	**$879**

Management uses EBITDA to assess operating performance and believes that it may assist users of our financial statements in analyzing the underlying trends in our business over time. Users

of our financial statements should consider this non-GAAP financial information in addition to, not as a substitute for, or as superior to, financial information prepared in accordance with GAAP. Our EBITDA included pre-tax charges of $1,112 million in 2005, $340 million in 2004 and $52 million in 2003.[2]

Operating Activities

Cash generated by our operating activities continues to provide a major source of funds for investing in our growth. The decrease in cash generated by our operating activities in 2005 as compared to 2004 is primarily attributable to the decrease in EBITDA and by changes in our operating assets and liabilities. The decrease in EBITDA in 2005 as compared to 2004 reflects our third quarter 2005 settlement with Medinol, which was partially offset by increased sales of our TAXUS stent system during 2005. We invested a portion of the cash from sales of our TAXUS stent system in our sales, clinical and manufacturing capabilities, and in research and development projects.

Significant cash flow effects from our operating assets and liabilities in 2005 included decreases in cash flow of: $162 million attributable to accounts payable and accrued expenses; $77 million attributable to inventories; $59 million attributable to prepaid expenses and other assets; and $45 million attributable to taxes payable and other liabilities. The decrease in accounts payable and accrued expenses in 2005 as compared to 2004 related to our $75 million provision for certain legal and regulatory matters, which included a civil settlement with the Department of Justice, and our one-time $110 million 401(k) contribution, which were both paid during June 2005. The increase in inventories in 2005 as compared to 2004 related primarily to the accumulation of inventory to fulfill worldwide demand for our TAXUS stent system and our Neuromodulation products. The increase in prepaid expenses and other assets in 2005 as compared to 2004 was attributable to the establishment of a tax-related receivable. The decrease in taxes payable and other liabilities in 2005 as compared to 2004 primarily related to $350 million in tax payments made during 2005 including those associated with cash repatriated under the American Jobs Creation Act and to the expected tax benefit associated with the settlement agreement with Medinol. The decrease in taxes payable in 2005 as compared to 2004 was partially offset by the increase in taxes payable associated with our 2005 earnings.

[2]The 2005 pre-tax charges consisted of a litigation settlement with Medinol; purchased research and development; costs that resulted from certain business optimization initiatives; and expenses related to certain retirement benefits. The 2004 pre-tax charges consisted of a provision for certain legal and regulatory matters, which included a civil settlement with the U.S. Department of Justice, an enhancement to our 401(k) Plan, purchased research and development and a non-cash charge resulting from certain modifications to our stock option plans. The 2003 pre-tax charges consisted of purchased research and development and charges related to litigation and product liability settlements.

Investing Activities

We made capital expenditures of $341 million in 2005 as compared to $274 million in 2004. The increase primarily related to capital spending to enhance our manufacturing and distribution capabilities. We expect to incur capital expenditures of approximately $400 million during 2006 (excluding Guidant), which includes additional capital expenditures to allow further growth in our Endosurgery group and Neuromodulation division, and certain business optimization initiatives in our human resources function, primarily outsourcing costs.

Our investing activities during 2005 also included: $178 million of net payments primarily attributable to our acquisitions of Rubicon, TriVascular and CryoVascular; $33 million of acquisition earn-out payments primarily associated with prior acquisitions; and $208 million of payments related to our strategic alliances with both privately held and publicly traded companies.

Financing Activities

Our cash flows from financing activities reflect proceeds from long-term public debt issuances; repayment of short-term borrowings; payments for share repurchases; and proceeds from option exercises related to our equity incentive programs.

The following table provides a summary at December 31 of our net debt:

(in millions)	2005	2004
Short-term debt	$ 156	$1,228
Long-term debt	1,864	1,139
Gross debt	**$2,020**	**$2,367**
Less: cash, cash equivalents and marketable securities	848	1,640
Net debt	**$1,172**	**$ 727**

We had outstanding borrowings of $2,020 million at December 31, 2005 at a weighted average interest rate of 4.80 percent as compared to outstanding borrowings of $2,367 million at December 31, 2004 at a weighted average interest rate of 3.38 percent. During 2005, we made net payments on borrowings of $313 million.

Our cash and cash equivalents are primarily held by our non-U.S. operations. In 2005, we repatriated approximately $1,046 million in extraordinary dividends as defined in the American Jobs Creation Act from our non-U.S. operations. The American Jobs Creation Act created a temporary incentive for U.S. corporations to repatriate accumulated income earned abroad by providing an

85 percent dividends received deduction for certain dividends from controlled foreign corporations. As of December 31, 2004, we had recorded a tax liability of $61 million for the amounts we intended to repatriate in 2005 under the American Jobs Creation Act.

In 2005, we repatriated earnings of non-U.S. subsidiaries that did not qualify under the American Jobs Creation Act. The resulting tax liabilities associated with this repatriation were $127 million. In addition, during 2005, we made a decision to repatriate additional amounts from certain of our non-U.S. operations. In connection with this decision, we established a deferred tax liability of $27 million that we believe is adequate to cover the taxes related to this repatriation.

Borrowings and Credit Arrangements

Revolving Credit Facilities

During 2005, we refinanced our revolving credit facilities to extend the maturity of one credit facility and to reduce borrowing capacity by $165 million. At December 31, 2005, our revolving credit facilities totaled approximately $2,020 million, as compared to $2,185 million at December 31, 2004. Our revolving credit facilities at December 31, 2005 consisted of a $1,500 million credit facility that terminates in May 2009; a $500 million credit facility that terminates in May 2010 and contains an option to increase the facility size by an additional $500 million in the future; and a $20 million uncommitted credit facility that terminates in May 2006. Our use of the borrowings is unrestricted and the borrowings are unsecured.

Our credit facilities provide us with borrowing capacity and support our commercial paper program. We had $149 million of commercial paper outstanding at December 31, 2005 at a weighted average interest rate of 4.11 percent and $280 million outstanding at December 31, 2004 at a weighted average interest rate of 2.44 percent. In September 2005, we repaid 45 billion Japanese yen (approximately $400 million) in credit facility borrowings outstanding at a weighted average interest rate of 0.37 percent.

During 2005, we decreased our credit and security facility that is secured by our U.S. trade receivables from $400 million to $100 million, effective April 30, 2005. During the first quarter of 2006, we expect to increase this facility from $100 million to $350 million. The credit and security facility terminates in August 2006. Borrowing availability under this facility changes based upon the amount of eligible receivables, concentration of eligible receivables and other factors. Certain significant changes in the quality of our receivables may require us to repay borrowings immediately under the facility. The credit agreement required us to create a wholly-owned entity, which is consolidated. This entity purchases our U.S. trade accounts receivable and then borrows from two third-party financial institutions using these receivables as collateral. The receivables and related borrowings remain on the balance sheet because we have the right to prepay any borrowings outstanding and effectively retain control over the receivables. Accordingly, pledged receivables are included as trade accounts receivable, net, while the corresponding borrowings are included as debt on the consolidated balance sheets. There were no outstanding borrowings under the revolving credit and security facility as of December 31, 2005 or December 31, 2004.

In addition, we have uncommitted credit facilities with two commercial Japanese banks that provide for borrowings and promissory notes discounting of up to 15 billion Japanese yen (translated to $127 million at December 31, 2005 and $145 million at December 31, 2004). Approximately $109 million of notes receivable were discounted at an average interest rate of 0.75 percent at December 31, 2005 and $128 million of notes receivable were discounted at an average interest rate of 0.75 percent at December 31, 2004.

As of December 31, 2005 and December 31, 2004, we intended to repay all of our short-term debt obligations within the next twelve-month period.

Senior Notes

We had senior notes of $1,850 million outstanding at December 31, 2005 and $1,600 million outstanding at December 31, 2004.

- In November 2005, we issued $400 million of senior notes due November 2015 (November 2015 Notes) and $350 million of senior notes due November 2035 (November 2035 Notes) under a $1,500 million shelf registration statement filed with the SEC in November 2004. The November 2015 Notes bear a semi-annual coupon of 5.50 percent, are redeemable prior to maturity and are not subject to any sinking fund requirements. The November 2035 Notes bear a semi-annual coupon of 6.25 percent, are redeemable prior to maturity and are not subject to any sinking fund requirements. These are publicly registered securities. In December 2005, we announced our intent to supplement the terms of our November 2015 Notes and November 2035 Notes to provide for a potential interest rate adjustment accruing from November 17, 2005 on each series of these senior notes in the event that our credit ratings are downgraded as a result of the closing of our

proposed acquisition of Guidant. The interest rate on these senior notes will be subject to a one-time increase based on our initial credit ratings. Based on preliminary indications from the rating agencies, we expect that the interest rate on each of our November 2015 Notes and our November 2035 Notes may increase by 0.75 percent. We will be unable to determine the actual increase, if any, of the interest rate on each of the November 2015 Notes and November 2035 Notes until after the closing of our proposed acquisition of Guidant. Any subsequent rating improvements will result in a decrease in the adjusted interest rate. The interest rate on the date these senior notes were originally issued will be permanently reinstated if and when the lowest credit ratings assigned to these senior notes is either A- or A3 or higher.

- In March 2005, we repaid $500 million of senior notes that were outstanding at December 31, 2004. The notes bore a semi-annual coupon of 6.625 percent, were not redeemable prior to maturity and were not subject to any sinking fund requirements.

- In November 2004, we issued $250 million of senior notes due January 2011 (January 2011 Notes) and $250 million of senior notes due January 2017 (January 2017 Notes) under a shelf registration statement filed with the SEC in November 2004. The January 2011 Notes bear a semi-annual coupon of 4.25 percent, are redeemable prior to maturity and are not subject to any sinking fund requirements. The January 2017 Notes bear a semi-annual coupon of 5.125 percent, are redeemable prior to maturity and are not subject to any sinking fund requirements. These senior notes are publicly registered securities. We entered into fixed-to-floating interest rate swaps indexed to six-month LIBOR, which approximated 4.70 percent at December 31, 2005 and 2.78 percent at December 31, 2004, to hedge against changes in the fair value of these senior notes.

- In June 2004, we issued $600 million of senior notes due June 2014 (June 2014 Notes) under a shelf registration statement filed with the SEC. The June 2014 Notes bear a semi-annual coupon of 5.45 percent, are redeemable prior to maturity and are not subject to any sinking fund requirements. These senior notes are publicly registered securities. We entered into fixed-to-floating interest rate swaps indexed to six-month LIBOR, which approximated 4.70 percent at December 31, 2005 and 2.78 percent at December 31, 2004, to hedge against changes in the fair value of these senior notes.

See *Market Risk Disclosures* for further discussion regarding the treatment of our interest rate swaps.

The remainder of our outstanding borrowings, including capital lease arrangements, was immaterial at December 31, 2005 and December 31, 2004.

Equity

We repurchased approximately 25 million shares of our common stock at an aggregate cost of $734 million in 2005, 10 million shares of our common stock at an aggregate cost of $360 million in 2004, and 22 million shares of our common stock at an aggregate cost of $570 million in 2003. Since 1992, we have repurchased approximately 132 million shares of our common stock and we have approximately 24 million shares of our common stock held in treasury at year end. Approximately 37 million shares remain under our previous share repurchase authorizations. Repurchased shares are available for reissuance under our equity incentive plans and for general corporate purposes, including strategic alliances and acquisitions.

During 2005, we received $94 million in proceeds from stock issuances related to our stock option and employee stock purchase plans. Proceeds from the exercise of employee stock options vary from period to period based upon, among other factors, fluctuations in the exercise patterns of employees.

Guidant Acquisition

At the effective time of the acquisition, each share of Guidant common stock will be converted into the right to receive (i) $42.00 in cash and (ii) a number of shares of Boston Scientific common stock equal to $38.00, subject to the calculation of the exchange ratio. See *Note O—Subsequent Events* to our 2005 consolidated financial statements included in this Annual Report for further details regarding the exchange ratio that will be used in determining the purchase price. Under the terms of the Abbott transaction agreement and at the closing of the Abbott transaction, Abbott has agreed to (1) pay an initial purchase price of $4.1 billion in cash plus potential future earn-out payments for the Guidant vascular and endovascular businesses, (2) make a five-year subordinated loan of $900 million to us at a 4.00 percent annual interest rate, and (3) purchase $1.4 billion in shares of Boston Scientific common stock.

In connection with the financing of the cash portion of the purchase price, various banks have committed to providing up to $14 billion in financing, which includes a $7 billion 364-day interim credit facility, a $5 billion five-year term loan facility and a $2 billion five-year revolving credit facility. The interim credit

facility, term loan and revolving credit facility will bear interest at LIBOR plus an interest margin between 0.30 percent (high A rating) and 0.85 percent (low BBB rating). The interest margin will be based on the highest two out of three of our long-term, senior unsecured, corporate credit ratings from Moody's Investor Service, Inc., Standard & Poor's Rating Services and Fitch Ratings. Of the $14 billion available pursuant to the commitment letter, we expect to borrow approximately $7.1 billion to finance the cash portion of the Guidant acquisition purchase price, which includes the $5 billion five-year term loan facility and $2.1 billion in borrowings under the 364-day interim credit facility. We also expect to use the $900 million loan from Abbott, for a total of $8 billion in borrowings to finance the cash portion of the purchase price. In 2006, we anticipate filing a new public registration statement with the SEC under which we intend to issue senior notes in order to refinance any borrowings outstanding under the interim credit facility and to register shares that we will issue to Abbott. The new five-year revolving credit facility will replace our existing $2 billion credit facilities. We also plan to use cash on hand and cash from the Abbott transaction to fund the cash portion of the Guidant purchase price. If the acquisition is completed, we intend to dedicate a significant portion of our future cash flow from operations to repay our outstanding debt obligations.

We currently have investment grade credit ratings. During February 2006, our credit rating was downgraded. The rating agencies have also indicated that they will further downgrade our credit ratings when the Guidant acquisition is consummated. However, we expect our credit ratings to remain at investment grade levels following the acquisition. Our credit ratings affect our cost of borrowings. If our credit ratings were to be downgraded below investment grade, our borrowing costs may increase and we may be subject to more stringent terms and conditions than those currently contained in our financing arrangements.

In addition, our authorized common stock will be increased from 1,200,000,000 shares to 2,000,000,000 shares in conjunction with our proposed acquisition of Guidant.

Contractual Obligations and Commitments

The following table provides a summary of certain information concerning our obligations and commitments to make future payments. See Notes D, F, H and O to our 2005 consolidated financial statements included in this Annual Report for additional information regarding our business combinations, long-term debt, lease arrangements, and subsequent events.

	Payments Due by Period				
(in millions)	1 Year or Less	2-3 Years	4-5 Years	After 5 Years	Total
Debt principal*	$156	$ 4	$ 2	$1,852	$2,014
Interest payments	100	200	200	846	1,346
Debt, including interest	256	204	202	2,698	3,360
Operating leases†	47	56	9	2	114
Purchase obligations†,††	102	15			117
Minimum royalty obligations††	3	6	4	8	21
Total	**$408**	**$281**	**$215**	**$2,708**	**$3,612**

* Debt as reported in our consolidated balance sheets includes the mark-to-market effect of our interest rate swaps and is net of the unamortized investor discount associated with the issuance of senior notes in conjunction with our various public debt offerings.

† In accordance with U.S. GAAP, these obligations are not reflected in our consolidated balance sheets.

†† These obligations related primarily to inventory commitments and capital expenditures entered in the normal course of business.

On January 25, 2006, we entered into a definitive agreement to acquire Guidant Corporation for an aggregate purchase price of $27 billion (net of proceeds from option exercises), which represents a combination of cash and stock worth $80 per share of Guidant common stock. In addition, in conjunction with the acquisition of Guidant, Abbott has agreed to acquire Guidant's vascular intervention and endovascular businesses. See *Note O—Subsequent Events* to our 2005 consolidated financial statements included in this Annual Report for further details regarding the transaction.

Certain of our business combinations involve the payment of contingent consideration. Certain of these payments are based on multiples of the acquired company's revenue during the earn-out period and, consequently, we cannot currently determine the total payments. However, we have developed an estimate of the maximum potential contingent consideration for each of our acquisitions with an outstanding earn-out obligation. At December 31, 2005, the estimated maximum potential amount of future contingent consideration (undiscounted) that we could be required to make associated with our business combinations is approximately $4 billion, some of which may be payable in our common stock. The milestones associated with the contingent consideration must be reached in certain future periods ranging

from 2006 through 2016. The estimated cumulative specified revenue level associated with these maximum future contingent payments is approximately $10 billion. Since it is not possible to estimate when, or even if, the acquired companies will reach their performance milestones or the amount of contingent consideration payable based on future revenues, the maximum contingent consideration has not been included in the table above.

In addition, we are currently considering the exercise of our option to acquire EndoTex Interventional Systems, Inc., a developer of stents used in the treatment of stenotic lesions in the carotid arteries. In conjunction with the acquisition of EndoTex, we would pay approximately $100 million in addition to our previous investments and notes issued of approximately $35 million, plus future consideration that is contingent upon EndoTex achieving certain performance-related milestones. Further, many of our equity investments give us the option to acquire the company in the future or require us to make certain payments that are contingent upon the company achieving certain product development targets or obtaining regulatory approvals. Since it is not possible to estimate when, or even if, we will exercise our option to acquire these companies or be required to make these contingent payments, we have not included future potential payments relating to these equity investments in the table above.

Critical Accounting Policies

We have adopted accounting policies to prepare our consolidated financial statements in conformity with U.S. GAAP. We describe these accounting polices in *Note A—Significant Accounting Policies* to our 2005 consolidated financial statements included in this Annual Report.

To prepare our consolidated financial statements in accordance with U.S. GAAP, management makes estimates and assumptions that may affect the reported amounts of our assets and liabilities, the disclosure of contingent assets and liabilities at the date of our financial statements and the reported amounts of our revenue and expenses during the reporting period. Our actual results may differ from these estimates.

These estimates are considered critical (1) if we are required to make assumptions about material matters that are uncertain at the time of estimation or (2) if materially different estimates could have been made or it is reasonably likely that the accounting estimate will change from period to period. The following are areas that we consider to be critical:

Revenue Recognition

Our revenue primarily consists of the sale of single-use medical devices. Revenue is considered to be realized or realizable and earned when all of the following criteria are met: persuasive evidence of a sales arrangement exists; delivery has occurred or services have been rendered; the price is fixed or determinable; and collectibility is reasonably assured. These criteria are generally met at the time of shipment when the risk of loss and title passes to the customer or distributor, unless a consignment arrangement exists. We recognize revenue from consignment arrangements based on product usage, which indicates that the sale is complete.

We generally allow our customers to return defective, damaged and, in certain cases, expired products for credit. Our estimate for sales returns is based upon contractual commitments and historical trends and is recorded as a reduction to revenue.

We offer sales rebates and discounts to certain customers. We treat sales rebates and discounts as a reduction of revenue and classify the corresponding liability as current. We estimate rebates for products where there is sufficient historical information available to predict the volume of expected future rebates. If we are unable to estimate the expected rebates reasonably, we record a liability for the maximum rebate percentage offered.

Inventories

We state inventories at the lower of first-in, first-out cost or market. We base our provisions for excess or expired inventory primarily on our estimates of forecasted net sales levels. A significant change in the timing or level of demand for our products as compared to forecasted amounts may result in recording additional provisions for excess or expired inventory in the future. We record provisions for inventory located in our manufacturing and distribution facilities as cost of sales. Consignment inventory write-downs are charged to selling, general and administrative expense and approximated $15 million in 2005, $10 million in 2004, and $8 million in 2003.

Valuation of Business Combinations

We record intangible assets acquired in recent business combinations under the purchase method of accounting. We allocate the amounts we pay for each acquisition to the assets we acquire and liabilities we assume based on their fair values at the dates of acquisition. We then allocate the purchase price in excess of net tangible assets acquired to identifiable intangible assets, including purchased research and development. The fair value of identifi-

able intangible assets is based on detailed valuations that use information and assumptions provided by management. We allocate any excess purchase price over the fair value of the net tangible and intangible assets acquired to goodwill. The use of alternative purchase price allocations and alternative estimated useful life assumptions could result in different intangible asset amortization expense in current and future periods.

The valuation of purchased research and development represents the estimated fair value at the dates of acquisition related to in-process projects. Our purchased research and development represents the value of in-process projects that have not yet reached technological feasibility and have no alternative future uses as of the date of acquisition. The primary basis for determining the technological feasibility of these projects is obtaining regulatory approval to market the underlying products in an applicable geographic region. We expense the value attributable to these in-process projects at the time of the acquisition. If the projects are not successful or completed in a timely manner, we may not realize the financial benefits expected for these projects, or for the acquisitions as a whole.

We use the income approach to determine the fair values of our purchased research and development. This approach determines fair value by estimating the after-tax cash flows attributable to an in-process project over its useful life and then discounting these after-tax cash flows back to a present value. We base our revenue assumptions on estimates of relevant market sizes, expected market growth rates, expected trends in technology and expected product introductions by competitors. In arriving at the value of the in-process projects, we consider, among other factors, the in-process projects' stage of completion, the complexity of the work completed as of the acquisition date, the costs already incurred, the projected costs to complete, the contribution of core technologies and other acquired assets, the expected introduction date and the estimated useful life of the technology. We base the discount rate used to arrive at a present value as of the date of acquisition on the time value of money and medical technology investment risk factors. For the in-process projects we acquired in connection with our recent acquisitions, we used the following risk-adjusted discount rates to discount our projected cash flows: in 2005, 18 percent to 27 percent; in 2004, 18 percent to 27 percent; and in 2003, 24 percent. We believe that the estimated purchased research and development amounts so determined represent the fair value at the date of acquisition and do not exceed the amount a third party would pay for the projects.

Amortization and Impairment of Intangible Assets

We record intangible assets at historical cost. We amortize our intangible assets subject to amortization, including patents, licenses, developed technology and core technology, using the straight-line method over their estimated useful lives. We review these intangible assets quarterly to determine if any adverse conditions exist or a change in circumstances has occurred that would indicate impairment or a change in their remaining useful life. We also review our indefinite-lived intangible assets at least annually for impairment by calculating the fair value of our assets and comparing the calculated fair values to the respective carrying values.

We test goodwill during the second quarter of each year for impairment, or more frequently if certain indicators are present or changes in circumstances suggest that impairment may exist. In performing the test, we calculate the fair value of the reporting units as the present value of estimated future cash flows using a risk-adjusted discount rate. The selection and use of an appropriate discount rate requires significant management judgment with respect to revenue and expense growth rates. We have not recorded impairment of goodwill in any of the years included in our consolidated statements of operations.

Investments in Strategic Alliances

As of December 31, 2005, we had investments in 66 strategic alliances totaling $594 million. As of December 31, 2004, we had investments in 58 strategic alliances totaling $529 million. These assets primarily represent investments in privately held and publicly traded equity securities. We account for investments in companies over which we have the ability to exercise significant influence under the equity method if we hold 50 percent or less of the voting stock. We account for investments in companies over which we do not have the ability to exercise significant influence under the cost method. Our determination of whether we have the ability to exercise significant influence over an investment requires judgment.

As of December 31, 2005, we held investments totaling $85 million in three companies that we accounted for under the equity method. Our ownership percentages in these companies range from approximately 21 percent to 28 percent. As of December 31, 2004, we held investments totaling $61 million in two companies that we accounted for under the equity method. Our ownership percentages in these companies range from approximately 25 percent to 30 percent.

Factors that we consider in determining whether we have the ability to exercise significant influence include, but are not limited to:

- our level of representation on the board of directors;
- our participation in the investee's policy making processes;
- transactions with the investee in the ordinary course of business;
- interchange of managerial personnel;
- the investee's technological dependency on us; and
- our ownership in relation to the concentration of other shareholdings.

For investments accounted for under the equity method, we initially record the investment at cost, and adjust the carrying amount to reflect our share of the earnings or losses of the investee, including all adjustments similar to those made in preparing consolidated financial statements. Amounts recorded to adjust the carrying amounts of investments accounted for under the equity method were not material to our statements of operations in 2005, 2004 or 2003. When we do not have the ability to exercise significant influence over an investee, we follow the cost method of accounting.

We regularly review our strategic alliance investments for impairment indicators. Examples of events or circumstances that may indicate that an investment is impaired include, but are not limited to, a significant deterioration in earnings performance; a significant adverse change in the regulatory, economic or technological environment of an investee; or a significant doubt about an investee's ability to continue as a going concern. If we determine that impairment exists and it is other-than-temporary, we will reduce the carrying value of the investment to its estimated fair value and will recognize an impairment loss in our consolidated statements of operations. Our exposure to loss related to our strategic alliances is generally limited to our equity investments, notes receivable and intangible assets associated with these alliances.

Income Taxes

We utilize the asset and liability method for accounting for income taxes. Under this method, we determine deferred tax assets and liabilities based on differences between the financial reporting and tax bases of our assets and liabilities. We measure deferred tax assets and liabilities using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

We recognized net deferred tax liabilities aggregating $110 million at December 31, 2005 and $18 million at December 31, 2004. The liabilities relate principally to deferred taxes associated with our acquisitions and earnings of our non-U.S. subsidiaries to be remitted in the future. The assets relate principally to the establishment of inventory and product-related reserves, purchased research and development, net operating loss carryforwards and tax credit carryforwards. In light of our historical financial performance, we believe these assets will be substantially recovered. See *Note I—Income Taxes* to our 2005 consolidated financial statements included in this Annual Report for a detailed analysis of our deferred tax positions.

We reduce our deferred tax assets by a valuation allowance if, based upon the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized. We consider relevant evidence, both positive and negative, to determine the need for a valuation allowance. Information evaluated includes our financial position and results of operations for the current and preceding years, as well as an evaluation of currently available information about future years.

We provide for income taxes payable related to earnings of our foreign subsidiaries that may be repatriated in the foreseeable future. Income taxes are not provided on the unremitted earnings of our foreign subsidiaries where such earnings have been permanently reinvested in our foreign operations. It is not practical to estimate the amount of income taxes payable on the earnings that are permanently reinvested in foreign operations. Unremitted earnings of our foreign subsidiaries that are permanently reinvested are $2,106 million at December 31, 2005 and $1,005 million at December 31, 2004.

We provide for potential amounts due in various tax jurisdictions. In the ordinary course of conducting business in multiple countries and tax jurisdictions, there are many transactions and calculations where the ultimate tax outcome is uncertain. Judgment is required in determining our worldwide income tax provision. In our opinion, adequate provisions for income taxes have been made for all years subject to audit. Although we believe our estimates are reasonable, no assurance can be given that the final tax outcome of these matters will not be different from that which is reflected in our historical income tax provisions and accruals. Such differences could have a material impact on our income tax provision and operating results in the period in which such determination is made.

Legal Costs

We are involved in various legal and regulatory proceedings, including intellectual property, breach of contract, securities litigation and product liability suits. In some cases, the claimants seek damages, as well as other relief, which, if granted, could require significant expenditures. We accrue costs of settlement, damages and, under certain conditions, costs of defense when a loss is deemed probable and such costs are estimable. Otherwise, we expense these costs as incurred. If the estimate of a probable loss is a range and no amount within the range is more likely, we accrue the minimum amount of the range. Our accrual for regulatory and litigation-related costs that were probable and estimable was $20 million at December 31, 2005 and $99 million at December 31, 2004. See further discussion of our individual material legal proceedings in *Note J—Commitments and Contingencies* to our 2005 consolidated financial statements included in this Annual Report. As of December 31, 2005, a range of loss associated with these individual material legal proceedings can not be estimated due to uncertainty surrounding the outcome of the proceedings.

Product Liability Costs and Securities Litigation Claims

We are substantially self-insured with respect to general, product liability and securities litigation claims. In the normal course of business, product liability and securities litigation claims are asserted against us. We accrue anticipated costs of litigation and loss for product liability and securities litigation claims based on historical experience, or to the extent specific losses are probable and estimable. We record losses for claims in excess of the limits of purchased insurance in earnings at the time and to the extent they are probable and estimable. Our accrual for product liability and securities litigation claims was $15 million at December 31, 2005 and $13 million at December 31, 2004. Product liability and securities litigation claims against us will likely be asserted in the future related to events not known to management at the present time. The absence of significant third-party insurance coverage increases our exposure to unanticipated claims or adverse decisions. However, based on product liability and securities litigation losses experienced in the past, our election to become substantially self-insured is not expected to have a material impact on our future operations.

Management believes that our risk management practices, including limited insurance coverage, are reasonably adequate to protect us against anticipated general, product liability and securities litigation losses. However, unanticipated catastrophic losses could have a material adverse impact on our financial position, results of operations and liquidity.

Costs Associated with Exit Activities

We accrue employee termination costs associated with an ongoing benefit arrangement if the obligation is attributed to prior services rendered, the rights to the benefits have vested and the payment is probable and the amount can be reasonably estimated. We generally record such costs into expense over the future service period, if any. In addition, in conjunction with an employee termination, we may offer voluntary termination benefits to employees. These benefits are recorded when the employee accepts the termination benefits and the amount can be reasonably estimated. Other costs associated with exit activities may include costs related to leased facilities to be abandoned or subleased and long-lived asset impairments.

During 2005, we recorded charges associated with exit activities of approximately $40 million. These charges included costs primarily attributable to employee terminations and outsourcing costs within our human resources function and international divisions; and a $10 million write-off of intangible assets related to our Enteryx Technology.

The recognition of charges associated with exit activities requires our management to make judgments and estimates regarding the nature, timing, and amount of costs associated with the planned exit activity. Management's estimates of future liabilities may change, requiring us to record additional restructuring charges or reduce the amount of liabilities already recorded. At the end of each reporting period, we evaluate the remaining accrued balances to ensure their adequacy, that no excess accruals are retained and that utilization of the provisions are for their intended purposes in accordance with developed exit plans.

New Accounting Standard

During 2004, the FASB issued Statement No. 123(R), *Share-Based Payment*, which is a revision of Statement No. 123, *Accounting for Stock-Based Compensation*. Statement No. 123(R) supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees* and amends Statement No. 95, *Statement of Cash Flows*. In general, Statement No. 123(R) contains similar accounting concepts as those described in Statement No. 123. However, Statement No. 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the consolidated statement of operations based on their fair values. Pro forma disclosure is no longer an alternative. Alternative phase-in methods are allowed under Statement No. 123(R). We adopted Statement No. 123(R) on its effective date of January 1, 2006 using the "modified-prospective method." Under this method, compensation cost is recognized (a) based on the requirements of Statement No. 123(R) for all

share-based payments granted on or after January 1, 2006 and (b) based on the requirements of Statement No. 123 for all unvested awards that were granted to employees prior to January 1, 2006. We expect to apply the Black-Scholes valuation model in determining the fair value of share-based payments to employees, which will then be amortized on a straight-line basis.

As permitted by Statement No. 123, for periods prior to January 1, 2006, we accounted for share-based payments to employees using Opinion No. 25's intrinsic value method and, as such, generally recognized no compensation cost for the granting of employee stock options, except as disclosed in *Note L—Stock Ownership Plans* to our 2005 consolidated financial statements contained in this Annual Report. Accordingly, the adoption of Statement No. 123(R)'s fair value method will negatively impact our statements of operations. The impact of adoption of Statement No. 123(R) cannot be quantified at this time because it will depend on the level of share-based payments granted in the future, expected volatilities and expected useful lives, among other factors, present at the grant date. However, had Statement No. 123(R) been effective in prior periods, the impact of that standard would have approximated the impact of Statement No. 123 as described in our disclosure of pro forma net income and net income per share in *Note A—Significant Accounting Policies* to our 2005 consolidated financial statements included in this Annual Report. Statement No. 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under currently effective accounting literature. This requirement will reduce net operating cash flows and increase net financing cash flows in periods after adoption of Statement No. 123(R). While we cannot estimate what those amounts will be in the future (because they depend on, among other things, when employees exercise stock options), the amount of operating cash flows recognized in prior periods for such excess tax deductions was $28 million in 2005, $185 million in 2004 and $154 million in 2003.

Further, most of our stock option awards provide for immediate vesting upon retirement, death or disability of the participant. We have traditionally accounted for the pro forma compensation expense related to stock-based awards made to retirement eligible individuals using the stated vesting period of the grant. This approach results in recognizing compensation expense over the vesting period except in the instance of the participant's actual retirement. Statement No. 123(R) clarified the accounting for stock-based awards made to retirement eligible individuals, which explicitly provides that the vesting period for a grant made to a retirement eligible employee is considered non-substantive and should be ignored when determining the period over which the award should be expensed. Upon adoption of SFAS No. 123(R), we will be required to expense stock-based awards over the period between grant date and retirement eligibility or immediately if the employee is retirement eligible at the date of grant. If we had historically accounted for stock-based awards made to retirement eligible individuals under these requirements, the pro forma expense disclosed in Note A would not have been materially impacted for the periods presented.

Market Risk Disclosures

We develop, manufacture and sell medical devices globally and our earnings and cash flow are exposed to market risk from changes in currency exchange rates and interest rates. We address these risks through a risk management program that includes the use of derivative financial instruments. We operate the program pursuant to documented corporate risk management policies. We do not enter into derivative transactions for speculative purposes. Gains and losses on derivative financial instruments substantially offset losses and gains on underlying hedged exposures. Furthermore, we manage our exposure to counterparty nonperformance on derivative instruments by entering into contracts with a diversified group of major financial institutions and by monitoring outstanding positions.

Our currency risk consists primarily of foreign currency denominated firm commitments, forecasted foreign currency denominated intercompany and third-party transactions and net investments in certain subsidiaries. We use both nonderivative (primarily European manufacturing operations) and derivative instruments to manage our earnings and cash flow exposure to changes in currency exchange rates. We had currency derivative instruments outstanding in the contract amount of $3,593 million at December 31, 2005 and $4,171 million at December 31, 2004. The decrease in the outstanding amount of our currency derivative instruments is primarily due to the maturity of hedge contracts. We recorded $176 million of other assets and $55 million of other liabilities to recognize the fair value of these derivative instruments at December 31, 2005 as compared to $70 million of other assets and $129 million of other liabilities recorded at December 31, 2004. A 10 percent appreciation in the U.S. dollar's value relative to the hedged currencies would increase the derivative instruments' fair value by $129 million at December 31, 2005 and by $163 million at December 31, 2004. A 10 percent depreciation in the U.S. dollar's value relative to the hedged currencies would decrease the derivative instruments' fair value by $157 million at December 31, 2005 and $190 million at December 31, 2004. Any increase or decrease in the fair value of our currency exchange rate sensitive derivative instruments would be substantially offset by a corresponding decrease or increase in the fair value of the hedged underlying asset, liability or cash flow.

Our earnings and cash flow are exposed to interest rate changes on U.S. dollar denominated debt partially offset by interest rate changes on U.S. dollar denominated cash investments. We use interest rate swaps to manage our exposure to interest rate movements and to reduce borrowing costs by converting either floating-rate debt into fixed-rate debt or fixed-rate debt into floating-rate debt. We had interest rate swaps outstanding in the notional amount of $1,100 million at December 31, 2005 and $1,600 million at December 31, 2004. Our interest rate swaps hedge against potential changes in the fair value of certain of our senior notes and are designated as fair value hedges. The decrease in the notional amount of our interest rate swaps is due to the maturing of hedge contracts related to our $500 million 6.625 percent senior notes, which we repaid upon maturity during March 2005. To recognize the fair value of these interest rate swaps, we recorded $21 million of other assets and $7 million of other liabilities at December 31, 2005 as compared to $32 million of other assets and $1 million of other liabilities at December 31, 2004. A one percentage point increase in global interest rates would decrease the derivative instruments' fair value by $74 million at December 31, 2005 as compared to $84 million at December 31, 2004. A one percentage point decrease in global interest rates would increase the derivative instruments' fair value by $80 million at December 31, 2005 as compared to $92 million at December 31, 2004. Any increase or decrease in the fair value of our interest rate sensitive derivative instruments would be substantially offset by a corresponding decrease or increase in the fair value of the hedged underlying liability.

Cautionary Statement for Purposes of the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995

Certain statements that we may make from time to time, including statements contained in this report and information incorporated by reference into this report, constitute "forward-looking statements." Forward-looking statements may be identified by words like "anticipate," "expect," "project," "believe," "plan," "estimate," "intend" and similar words used in connection with, among other things, discussions of our financial performance, growth strategy, regulatory approvals, product development or new product launches, market position, sales efforts, intellectual property matters or acquisitions and divestitures. These forward-looking statements are based on our beliefs, assumptions and estimates using information available to us at the time and are not intended to be guarantees of future events or performance. If our underlying assumptions turn out to be incorrect, or if certain risks or uncertainties materialize, actual results could vary materially from the expectations and projections expressed or implied by our forward-looking statements. As a result, investors are cautioned not to place undue reliance on any of our forward-looking statements.

We do not intend to update these forward-looking statements below even if new information becomes available or other events occur in the future. We have identified these forward-looking statements below in order to take advantage of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Certain factors that could cause actual results to differ materially from those expressed in forward-looking statements are contained below.

Coronary Stents

- Volatility in the coronary stent market, competitive offerings and the timing of receipt of regulatory approvals to market existing and anticipated drug-eluting stent technology and other coronary and peripheral stent platforms;
- Our ability to launch our TAXUS® Express² coronary stent system in Japan during the first half of 2007, and to launch our next-generation drug-eluting stent system, the TAXUS® Liberté™ coronary stent system, in the U.S. during the second half of 2006 and to maintain or expand our worldwide market leadership positions through reinvestment in our drug-eluting stent program;
- The continued availability of our TAXUS stent system in sufficient quantities and mix, our ability to prevent disruptions to our TAXUS stent system manufacturing processes and to maintain or replenish inventory levels consistent with forecasted demand around the world as we transition to next-generation stent products;
- The impact of new drug-eluting stents on the size of the coronary stent market, distribution of share within the coronary stent market in the U.S. and around the world, the average number of stents used per procedure and average selling prices;
- The overall performance of and continued physician confidence in our and other drug-eluting stents and the results of drug-eluting stent clinical trials undertaken by us, our competitors or other third parties;
- Continued growth in the rate of physician adoption of drug-eluting stent technology in our Europe and Inter-Continental markets;
- Our ability to take advantage of our position as one of two early entrants in the U.S. drug-eluting stent market, to anticipate competitor products as they enter the market and to respond to the challenges presented as additional competitors enter the U.S. drug-eluting stent market; and
- Our ability to manage inventory levels, accounts receivable, gross margins and operating expenses relating to our TAXUS stent system and other product franchises and to react effectively to worldwide economic and political conditions.

Litigation and Regulatory Compliance

- The effect of litigation, risk management practices, including self-insurance, and compliance activities on our loss contingency, legal provision and cash flow;
- The impact of stockholder derivative and class action, patent, product liability and other litigation; and
- Any conditions imposed in resolving, or any inability to resolve, outstanding warning letters or other FDA matters, as well as risks generally associated with regulatory compliance, quality systems standards and complaint-handling.

Innovation

- Our ability successfully to complete planned clinical trials, to obtain regulatory approvals and to develop and launch products on a timely basis within cost estimates, including the successful completion of in-process projects from purchased research and development;
- Our ability to manage research and development and other operating expenses consistent with our expected revenue growth over the next twelve months;
- Our ability to fund and achieve benefits from our focus on internal research and development and external alliances as well as our ability to capitalize on opportunities across our businesses;
- Our ability to develop products and technologies successfully in addition to our TAXUS coronary stent technology;
- Our failure to succeed at, or our decision to discontinue, any of our growth initiatives;
- Our ability to integrate the acquisitions and other strategic alliances we have consummated;
- Our decision to exercise options to purchase certain companies party to our strategic alliances and our ability to fund with cash or common stock these and other acquisitions; and
- The timing, size and nature of strategic initiatives, market opportunities and research and development platforms available to us and the ultimate cost and success of these initiatives.

International Markets

- Increasing dependence on international sales to achieve growth;
- Risks associated with international operations including compliance with local legal and regulatory requirements; and
- The potential effect of foreign currency fluctuations and interest rate fluctuations on our revenues, expenses and resulting margins.

Liquidity

- Our ability to generate sufficient cash flow to fund operations and capital expenditures, as well as our strategic investments over the next twelve months and to maintain borrowing flexibility beyond the next twelve months;
- Our ability to access the public capital markets and to issue debt or equity securities on terms reasonably acceptable to us;
- Our ability to achieve a 23 percent effective tax rate, excluding certain charges, during 2006 and to recover substantially all of our deferred tax assets; and
- Our ability to align expenses with future expected revenue levels and reallocate resources to support our future growth.

Other

- Risks associated with significant changes made or to be made to our organizational structure or to the membership of our executive committee; and
- Risks associated with our proposed acquisition of Guidant Corporation, including, among other things, the indebtedness we will incur and the integration challenges we will face after consummation of the acquisition.

Several important factors, in addition to the specific factors discussed in connection with each forward-looking statement individually, could affect our future results and growth rates and could cause those results and rates to differ materially from those expressed in the forward-looking statements contained in this report. These additional factors include, among other things, future economic, competitive, reimbursement and regulatory conditions, new product introductions, demographic trends, intellectual property, financial market conditions and future business decisions made by us and our competitors, all of which are difficult or impossible to predict accurately and many of which are beyond our control. Therefore, we wish to caution each reader of this report to consider carefully these factors as well as the specific factors discussed with each forward-looking statement in this report and as disclosed in our filings with the SEC. These factors, in some cases, have affected and in the future (together with other factors) could affect our ability to implement our business strategy and may cause actual results to differ materially from those contemplated by the statements expressed in this report.

As the management of Boston Scientific Corporation, we are responsible for establishing and maintaining adequate internal control over financial reporting. We designed our internal control system to provide reasonable assurance to management and the Board of Directors regarding the preparation and fair presentation of our financial statements.

We assessed the effectiveness of our internal control over financial reporting as of December 31, 2005. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control—Integrated Framework. Based on our assessment, we believe that, as of December 31, 2005, our internal control over financial reporting is effective at a reasonable assurance level based on these criteria.

Ernst & Young LLP, an independent registered public accounting firm, has issued an audit report on management's assessment of internal control over financial reporting and on the effectiveness of our internal control over financial reporting. This report in which they expressed an unqualified opinion is included below.

James R. Tobin
President and Chief Executive Officer

Lawrence C. Best
Executive Vice President and Chief Financial Officer

The Board of Directors and Stockholders of Boston Scientific Corporation

We have audited management's assessment, included in the accompanying Management's Report on Internal Control over Financial Reporting, that Boston Scientific Corporation maintained effective internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Boston Scientific Corporation's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the company's internal control over financial reporting based on our audit.

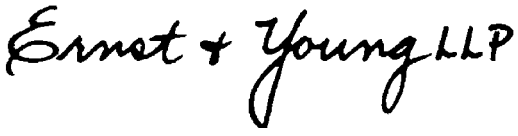
We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

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

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

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Boston Scientific Corporation as of December 31, 2005 and December 31, 2004, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2005 of Boston Scientific Corporation and our report dated February 24, 2006, expressed an unqualified opinion thereon.



Boston, Massachusetts
February 24, 2006

CONSOLIDATED STATEMENTS OF OPERATIONS (in millions, except per share data)

Year Ended December 31,	2005	2004	2003
Net sales	$6,283	$5,624	$3,476
Cost of products sold	1,386	1,292	961
Gross profit	**4,897**	**4,332**	**2,515**
Selling, general and administrative expenses	1,814	1,742	1,171
Research and development expenses	680	569	452
Royalty expense	227	195	54
Amortization expense	152	112	89
Litigation-related charges	780	75	15
Purchased research and development	276	65	37
Total operating expenses	**3,929**	**2,758**	**1,818**
Operating income	**968**	**1,574**	**697**
Other income (expense):			
Interest expense	(90)	(64)	(46)
Other, net	13	(16)	(8)
Income before income taxes	**891**	**1,494**	**643**
Income taxes	263	432	171
Net income	**$ 628**	**$1,062**	**$ 472**
Net income per common share—basic	**$ 0.76**	**$ 1.27**	**$ 0.57**
Net income per common share—assuming dilution	**$ 0.75**	**$ 1.24**	**$ 0.56**

(See notes to the consolidated financial statements)

CONSOLIDATED BALANCE SHEETS (in millions)

As of December 31,	2005	2004
Assets		
Current assets		
Cash and cash equivalents	$ 689	$1,296
Marketable securities	159	344
Trade accounts receivable, net	932	900
Inventories	418	360
Deferred income taxes	152	241
Prepaid expenses and other current assets	281	148
Total current assets	**2,631**	**3,289**
Property, plant and equipment, net	1,011	870
Investments	594	529
Other assets	225	142
Intangible assets		
Goodwill	1,938	1,712
Technology—core, net	1,099	942
Technology—developed, net	209	200
Patents, net	338	339
Other intangible assets, net	151	147
Total intangible assets	**3,735**	**3,340**
	$8,196	**$8,170**

(See notes to the consolidated financial statements)

CONSOLIDATED BALANCE SHEETS (in millions, except share data)

As of December 31,	2005	2004
Liabilities and Stockholders' Equity		
Current liabilities		
Commercial paper	$ 149	$ 280
Current maturities of long-term debt	1	502
Bank obligations	6	446
Accounts payable	105	108
Accrued expenses	1,124	902
Income taxes payable	17	255
Other current liabilities	77	112
Total current liabilities	**1,479**	**2,605**
Long-term debt	1,864	1,139
Deferred income taxes	262	259
Other long-term liabilities	309	142
Commitments and contingencies		
Stockholders' equity		
Preferred stock, $.01 par value—authorized 50,000,000 shares, none issued and outstanding		
Common stock, $.01 par value—authorized 1,200,000,000 shares, 844,565,292 shares issued at December 31, 2005 and December 31, 2004	8	8
Additional paid-in capital	1,658	1,633
Deferred compensation	(98)	(2)
Treasury stock, at cost—24,215,559 shares at December 31, 2005 and 9,221,468 shares at December 31, 2004	(717)	(320)
Retained earnings	3,410	2,790
Accumulated other comprehensive income (loss)		
Foreign currency translation adjustment	(71)	(34)
Unrealized gain on available-for-sale securities, net	26	2
Unrealized gain (loss) on derivative financial instruments, net	67	(51)
Minimum pension liability	(1)	(1)
Total stockholders' equity	**4,282**	**4,025**
	$8,196	**$8,170**

(See notes to the consolidated financial statements)

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (in millions, except share data)

	Common Stock		Additional Paid-In Capital	Deferred Compensation	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Comprehensive Income (Loss)
	Shares Issued	Par Value						
Balance at December 31, 2002	**414,882,413**	**$4**	**$1,250**		**$ (54)**	**$1,394**	**$(127)**	
Comprehensive income								
Net income						472		$ 472
Other comprehensive income (expense), net of tax								
Foreign currency translation adjustment							69	69
Net change in equity investments							52	52
Net change in derivative financial instruments							(44)	(44)
Net change in minimum pension liability							1	1
Issuance of common stock			(179)		512	(73)		
Issuance of restricted stock, net of cancellations				(1)	1			
Stock split effected in the form of a stock dividend	414,882,413	4				(4)		
Repurchases of common stock					(570)			
Tax benefit related to stock options			154					
Amortization of deferred compensation				1				
Balance at December 31, 2003	**829,764,826**	**8**	**1,225**		**(111)**	**1,789**	**(49)**	**$ 550**
Comprehensive income								
Net income						1,062		$1,062
Other comprehensive income (expense), net of tax								
Foreign currency translation adjustment							16	16
Net change in equity investments							(48)	(48)
Net change in derivative financial instruments							(3)	(3)
Issuance of common stock	14,800,466		132		149	(56)		
Issuance of restricted stock, net of cancellations			1	(3)	2			
Repurchases of common stock					(360)			
Tax benefit related to stock options			185					
Step-up accounting adjustment for certain investments						(5)		
Stock-compensation charge for certain modifications			90					
Amortization of deferred compensation				1				
Balance at December 31, 2004	**844,565,292**	**8**	**1,633**	**(2)**	**(320)**	**2,790**	**(84)**	**$1,027**
Comprehensive income								
Net income						628		$ 628
Other comprehensive income (expense), net of tax								
Foreign currency translation adjustment							(37)	(37)
Net change in equity investments							24	24
Net change in derivative financial instruments							118	118
Issuance of common stock			(113)		207			
Common stock issued for acquisitions			(5)		129			
Issuance of restricted stock, net of cancellations			114	(115)	1			
Repurchases of common stock					(734)			
Tax benefit related to stock options			28					
Step-up accounting adjustment for certain investments						(8)		
Amortization of deferred compensation			1	19				
Balance at December 31, 2005	**844,565,292**	**$8**	**$1,658**	**$ (98)**	**$(717)**	**$3,410**	**$ 21**	**$ 733**

(See notes to the consolidated financial statements)

CONSOLIDATED STATEMENTS OF CASH FLOWS (in millions)

Year Ended December 31,	2005	2004	2003
Operating Activities			
Net income	$ 628	$ 1,062	$ 472
Adjustments to reconcile net income to cash provided by operating activities:			
Gain on sale of equity investments	(4)	(36)	
Depreciation and amortization	314	275	196
Deferred income taxes	4	30	(31)
Purchased research and development	276	65	37
Tax benefit relating to stock options	28	185	154
Stock-compensation expense, including expense for certain modifications	13	62	1
Increase (decrease) in cash flows from operating assets and liabilities, excluding the effect of acquisitions:			
Trade accounts receivable	(24)	(317)	(74)
Inventories	(77)	(57)	(21)
Prepaid expenses and other assets	(59)	(15)	6
Accounts payable and accrued expenses	(162)	362	85
Income taxes payable and other liabilities	(45)	200	(19)
Other, net	11	(12)	(19)
Cash provided by operating activities	903	1,804	787
Investing Activities			
Property, plant and equipment			
Purchases	(341)	(274)	(188)
Proceeds on disposals	19		1
Marketable securities			
Purchases	(56)	(660)	(130)
Proceeds from maturities	241	397	66
Acquisitions			
Payments for acquisitions of businesses, net of cash acquired	(178)	(804)	(13)
Payments relating to prior year acquisitions	(33)	(107)	(283)
Strategic alliances			
Purchases of publicly traded equity securities	(52)	(23)	(105)
Payments for investments in privately held companies and acquisitions of certain technologies	(156)	(249)	(220)
Proceeds from sales of privately held and publicly traded equity securities	5	98	1
Cash used for investing activities	(551)	(1,622)	(871)
Financing Activities			
Debt			
Net (payments on) proceeds from commercial paper	(131)	(723)	915
Payments on notes payable, capital leases and long-term borrowings	(508)	(17)	(8)
Proceeds from notes payable and long-term borrowings, net of debt issuance costs	739	1,092	2
Net (payments on) proceeds from borrowings on revolving credit facilities	(413)	225	(116)
Equity			
Repurchases of common stock	(734)	(360)	(570)
Proceeds from issuances of shares of common stock	94	225	260
Other, net	(1)	(3)	4
Cash (used for) provided by financing activities	(954)	439	487
Effect of foreign exchange rates on cash	(5)	4	8
Net (decrease) increase in cash and cash equivalents	(607)	625	411
Cash and cash equivalents at beginning of year	1,296	671	260
Cash and cash equivalents at end of year	**$ 689**	**$ 1,296**	**$ 671**
Supplemental cash flow information			
Cash paid during the year for:			
Income taxes	$ 350	$ 72	$ 30
Interest	87	61	52

(See notes to the consolidated financial statements)

Note A – Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of Boston Scientific Corporation (the Company) and its subsidiaries, substantially all of which the Company wholly owns. The Company considers the principles of Financial Accounting Standards Board (FASB) Interpretation (FIN) No. 46, *Consolidation of Variable Interest Entities* and Accounting Research Bulletin No. 51, *Consolidation of Financial Statements* when determining whether an entity is subject to consolidation. The Company accounts for investments in companies over which it has the ability to exercise significant influence under the equity method if the Company holds 50 percent or less of the voting stock.

Accounting Estimates

The preparation of financial statements in conformity with United States generally accepted accounting principles (U.S. GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash, Cash Equivalents and Marketable Securities

Cash and cash equivalents are recorded in the consolidated balance sheets at cost, which approximates fair value. The Company considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents.

The Company invests excess cash in high-quality marketable securities consisting primarily of corporate notes and bank time deposits. As of December 31, 2005 and December 31, 2004, the Company classified its cash investments as available-for-sale. The Company records available-for-sale investments at fair value. Unrealized gains and temporary losses on available-for-sale securities are excluded from earnings and are reported, net of tax, as a separate component of stockholders' equity until realized. The Company bases the cost of available-for-sale securities on the specific identification method. Realized gains and losses on sales of available-for-sale securities are computed based upon initial cost adjusted for any other-than-temporary declines in fair value. The Company records held-to-maturity securities at amortized cost and adjusts for amortization of premiums and accretion of discounts to maturity. Investments in debt securities or equity securities that have a readily determinable fair value that are bought and held principally for selling them in the near term are classified as trading securities. None of the Company's investments are considered trading or held-to-maturity securities at December 31, 2005 and December 31, 2004.

Cash, cash equivalents and marketable securities at December 31 consist of the following:

(in millions)	2005	2004
Cash and cash equivalents	$689	$1,296
Marketable securities (maturing 91 days-1 year)		
Available-for-sale	159	344
	$848	**$1,640**

The amortized cost of marketable securities approximated their fair value at December 31, 2005 and December 31, 2004.

Concentrations of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents, marketable securities, derivative financial instrument contracts and accounts receivable. The Company's investment policy limits exposure to concentrations of credit risk and changes in market conditions. Counterparties to financial instruments expose the Company to credit-related losses in the event of nonperformance. The Company transacts its financial instruments with a diversified group of major financial institutions and monitors outstanding positions to limit its credit exposure.

The Company provides credit, in the normal course of business, to hospitals, healthcare agencies, clinics, doctors' offices and other private and governmental institutions. The Company performs ongoing credit evaluations of its customers and maintains allowances for potential credit losses.

Revenue Recognition

The Company's revenue primarily consists of the sale of single-use medical devices. Revenue is considered to be realized or realizable and earned when all of the following criteria are met: persuasive evidence of a sales arrangement exists; delivery has occurred or services have been rendered; the price is fixed or determinable; and collectibility is reasonably assured. These criteria are generally met at the time of shipment when the risk of loss and title passes to the customer or distributor, unless a consignment arrangement exists. The Company recognizes revenue from consignment arrangements based on product usage, which indicates that the sale is complete.

The Company generally allows its customers to return defective, damaged and, in certain instances, expired products for credit. The estimate for sales returns is based upon contractual

commitments and historical trends and is recorded as a reduction to revenue.

The Company offers sales rebates and discounts to certain customers. The Company treats sales rebates and discounts as a reduction of revenue and classifies the corresponding liability as current. The Company estimates rebates for products where there is sufficient historical information available to predict the volume of expected future rebates. If the Company is unable to estimate the expected rebates reasonably, it records a liability for the maximum rebate percentage offered.

The Company has entered certain agreements with group purchasing organizations to sell its products to participating hospitals at pre-negotiated prices. Revenue generated from these agreements is recognized following the same revenue recognition criteria discussed above.

Inventories

The Company states inventories at the lower of first-in, first-out cost or market. Provisions for excess or expired inventory are primarily based on management's estimates of forecasted net sales levels. A significant change in the timing or level of demand for the Company's products as compared to forecasted amounts may result in recording additional provisions for excess or expired inventory in the future. The Company records provisions for inventory located in its manufacturing and distribution facilities as cost of sales. Consignment inventory write-downs are charged to selling, general and administrative expense and approximated $15 million in 2005, $10 million in 2004, and $8 million in 2003.

Property, Plant and Equipment

The Company states property, plant, equipment and leasehold improvements at historical cost. Expenditures for maintenance and repairs are charged to expense; additions and improvements are capitalized. The Company generally provides for depreciation using the straight-line method at rates that approximate the estimated useful lives of the assets. Buildings and improvements are depreciated over a 20 to 40 year life; equipment, furniture and fixtures are depreciated over a 3 to 7 year life; leasehold improvements are amortized on a straight-line basis over the shorter of the useful life of the improvement or the term of the lease.

Valuation of Business Combinations

The Company records intangible assets acquired in recent business combinations under the purchase method of accounting. The Company accounts for acquisitions completed before July 1, 2001 in accordance with Accounting Principles Board (APB) Opinion No. 16, *Business Combinations* and accounts for acquisitions completed after June 30, 2001 in accordance with FASB Statement No. 141, *Business Combinations*. Amounts paid for each acquisition are allocated to the assets acquired and liabilities assumed based on their fair values at the dates of acquisition. The Company then allocates the purchase price in excess of net tangible assets acquired to identifiable intangible assets, including purchased research and development. The fair value of identifiable intangible assets is based on detailed valuations that use information and assumptions provided by management. The Company allocates any excess purchase price over the fair value of the net tangible and intangible assets acquired to goodwill.

The valuation of purchased research and development represents the estimated fair value at the dates of acquisition related to in-process projects. The Company's purchased research and development represents the value of in-process projects that have not yet reached technological feasibility and have no alternative future uses as of the date of acquisition. The primary basis for determining the technological feasibility of these projects is obtaining regulatory approval to market the underlying products in an applicable geographic region. The Company expenses the value attributable to these in-process projects at the time of the acquisition. If the projects are not successful or completed in a timely manner, the Company may not realize the financial benefits expected for these projects, or for the acquisitions as a whole. In addition, the Company records certain costs associated with its strategic alliances as purchased research and development.

The Company uses the income approach to determine the fair values of its purchased research and development. This approach determines fair value by estimating the after-tax cash flows attributable to an in-process project over its useful life and then discounting these after-tax cash flows back to a present value. The Company bases its revenue assumptions on estimates of relevant market sizes, expected market growth rates, expected trends in technology and expected product introductions by competitors. In arriving at the value of the in-process projects, the Company considers, among other factors, the in-process projects' stage of completion, the complexity of the work completed as of the acquisition date, the costs already incurred, the projected costs to complete, the contribution of core technologies and other acquired assets, the expected introduction date and the estimated useful life of the technology. The Company bases the discount rate used to arrive at a present value as of the date of acquisition on the time value of money and medical technology investment risk factors. For the in-process projects the Company acquired in connection with its recent acquisitions, it used the

following risk-adjusted discount rates to discount its projected cash flows: in 2005, 18 percent to 27 percent; in 2004, 18 percent to 27 percent; and in 2003, 24 percent. The Company believes that the estimated purchased research and development amounts so determined represent the fair value at the date of acquisition and do not exceed the amount a third party would pay for the projects.

Amortization and Impairment of Intangible Assets

The Company records intangible assets at historical cost. The Company amortizes its intangible assets using the straight-line method over their estimated useful lives as follows: patents and licenses, 2 to 20 years; definite-lived core and developed technology, 5 to 25 years; other intangible assets, various. The Company reviews intangible assets subject to amortization quarterly to determine if any adverse conditions exist or a change in circumstances has occurred that would indicate impairment or a change in the remaining useful life. Conditions that would indicate impairment and trigger a more frequent impairment assessment include, but are not limited to, a significant adverse change in legal factors or business climate that could affect the value of an asset, or an adverse action or assessment by a regulator. If the carrying value of an asset exceeds its undiscounted cash flows, the Company writes-down the carrying value of the intangible asset to its fair value in the period identified. The Company generally calculates fair value as the present value of estimated future cash flows to be generated by the asset using a risk-adjusted discount rate. If the estimate of an intangible asset's remaining useful life is changed, the Company amortizes the remaining carrying value of the intangible asset prospectively over the revised remaining useful life. In addition, the Company reviews its indefinite-lived intangible assets at least annually for impairment and reassesses their classification as indefinite-lived assets. To test for impairment, the Company calculates the fair value of its indefinite-lived intangible assets and compares the calculated fair values to the respective carrying values. Impairments of intangible assets are recorded as amortization expense in the consolidated statements of operations.

The Company tests goodwill during the second quarter of each year for impairment, or more frequently if certain indicators are present or changes in circumstances suggest that impairment may exist. When conducting its annual goodwill impairment test, the Company utilizes the two-step approach prescribed under FASB Statement No. 142, *Goodwill and Other Intangible Assets*. The first step requires a comparison of the carrying value of the reporting units, as defined, to the fair value of these units. As of December 31, 2005, the Company identified its seven domestic divisions, which in aggregate make up the U.S. operating segment, and its three international operating segments as its reporting units for purposes of the goodwill impairment test. To derive the carrying value of its reporting units, at the time of acquisition, the Company assigns goodwill to the reporting units that it expects to benefit from the respective business combination. In addition, assets and liabilities, including corporate assets, which relate to a reporting unit's operations and would be considered in determining fair value, are allocated to the individual reporting units. Assets and liabilities not directly related to a specific reporting unit, but from which the reporting unit benefits, are primarily allocated based on the respective revenue contribution of each reporting unit. If the carrying value of a reporting unit exceeds its fair value, the Company will perform the second step of the goodwill impairment test to measure the amount of impairment loss, if any. The second step of the goodwill impairment test compares the implied fair value of a reporting unit's goodwill with its carrying value. Since the adoption of Statement No. 142, the Company has not performed the second step of the impairment test because the fair value of each reporting unit has exceeded its respective carrying value.

Investments in Strategic Alliances

The Company accounts for its publicly traded investments as available-for-sale securities based on the quoted market price at the end of the reporting period. The Company accounts for its investments for which fair value is not readily determinable in accordance with APB Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock*, Emerging Issues Task Force No. 02-14, *Whether an Investor Should Apply the Equity Method of Accounting to Investments other than Common Stock* and FASB Staff Position No. 115-1 and 124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*.

The Company accounts for investments over which it has the ability to exercise significant influence over the investee's operating and financial policies under the equity method if the Company holds 50 percent or less of the voting stock. Factors that management considers in determining whether the Company has the ability to exercise significant influence include, but are not limited to:

- The level of representation on the board of directors of the investee;
- participation in the investee's policy making processes;

- transactions with the investee in the ordinary course of business;
- interchange of managerial personnel;
- the investee's technological dependency on the Company; and
- the Company's ownership in relation to the concentration of other shareholdings.

For investments accounted for under the equity method, the Company initially records the investment at cost, and adjusts the carrying amount to reflect the Company's share of the earnings or losses of the investee, including all adjustments similar to those made in preparing consolidated financial statements. Amounts recorded to adjust the carrying amounts of investments accounted for under the equity method were not material to the Company's consolidated statements of operations in 2005, 2004 or 2003. When the Company does not have the ability to exercise significant influence over an investee, the Company follows the cost method of accounting.

Each reporting period, the Company evaluates its investments for impairment if an event or circumstance occurs that is likely to have a significant adverse effect on the fair value of the investment. Examples of such events or circumstances include, but are not limited to, a significant deterioration in earnings performance; a significant adverse change in the regulatory, economic or technological environment of an investee; or a significant doubt about an investee's ability to continue as a going concern. If the Company identifies an impairment indicator, the Company will estimate the fair value of the investment and compare it to its carrying value. If the fair value of the investment is less than its carrying value, the investment is impaired and the Company makes a determination as to whether the impairment is other-than-temporary. Impairment is deemed other-than-temporary unless the Company has the ability and intent to hold an investment for a period sufficient for a market recovery up to the carrying value of the investment. Further, evidence must indicate that the carrying value of the investment is recoverable within a reasonable period. For an other-than-temporary impairment, the Company recognizes an impairment loss equal to the difference between an investment's carrying value and its fair value. Impairment losses on these investments are included in other, net in the consolidated statements of operations.

Income Taxes

The Company utilizes the asset and liability method for accounting for income taxes. Under this method, the Company determines deferred tax assets and liabilities based on differences between the financial reporting and tax bases of its assets and liabilities. The Company measures deferred tax assets and liabilities using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

The Company reduces its deferred tax assets by a valuation allowance if, based upon the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The Company considers relevant evidence, both positive and negative, to determine the need for a valuation allowance. Information evaluated includes the Company's financial position and results of operations for the current and preceding years, as well as an evaluation of currently available information about future years.

The Company provides for income taxes payable related to earnings of its foreign subsidiaries that may be repatriated in the foreseeable future. Income taxes are not provided on the unremitted earnings of the Company's foreign subsidiaries where such earnings have been permanently reinvested in its foreign operations. It is not practical to estimate the amount of income taxes payable on the earnings that are permanently reinvested in foreign operations. Unremitted earnings of the Company's foreign subsidiaries that are permanently reinvested are $2,106 million at December 31, 2005 and $1,005 million at December 31, 2004.

The Company provides for potential amounts due in various tax jurisdictions. In the ordinary course of conducting business in multiple countries and tax jurisdictions, there are many transactions and calculations where the ultimate tax outcome is uncertain. Judgment is required in determining the Company's worldwide income tax provision. In management's opinion, adequate provisions for income taxes have been made for all years subject to audit.

Legal Costs

The Company is involved in various legal and regulatory proceedings, including intellectual property, breach of contract, securities litigation and product liability suits. In some cases, the claimants seek damages, as well as other relief, which, if granted, could require significant expenditures. In accordance with FASB Statement No. 5, *Accounting for Contingencies*, the Company accrues costs of settlement, damages and, under certain conditions, costs of defense when a loss is deemed probable and such costs are estimable. Otherwise, these expenses are expensed as incurred.

If the estimate of a probable loss is a range and no amount within the range is more likely, the Company accrues the minimum amount of the range. The Company's accrual for regulatory and litigation-related costs that were probable and estimable was $20 million at December 31, 2005 and $99 million at December 31, 2004. As of December 31, 2005, a range of loss associated with the individual material legal proceedings discussed in *Note J—Commitments and Contingencies* cannot be estimated due to the uncertainty surrounding the outcome of the proceedings.

Product Liability Costs and Securities Liability Claims

The Company is substantially self-insured with respect to general, product liability and securities litigation claims. In the ordinary course of business, product liability and securities litigation claims are asserted against us. The Company accrues anticipated costs of litigation and loss for product liability and securities litigation claims based on historical experience, or to the extent specific losses are probable and estimable. The Company records losses for claims in excess of the limits of purchased insurance in earnings at the time and to the extent they are probable and estimable. The accrual for product liability and securities litigation claims was $15 million at December 31, 2005 and $13 million at December 31, 2004.

Warranty Obligations

The Company estimates the costs that may be incurred under its warranties based on historical experience and records a liability at the time the product is sold. Factors that affect the Company's warranty liability include the number of units sold, the historical and anticipated rates of warranty claims and the cost per claim. The Company regularly assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary. Expense attributable to warranties was not material to the statements of operations for 2005, 2004 and 2003.

Costs Associated with Exit Activities

The Company records employee termination costs in accordance with FASB Statement No. 112, *Employer's Accounting for Post Employment Benefits*, if the benefits are paid as part of an ongoing benefit arrangement, which includes benefits provided as part of Boston Scientific's domestic severance policy or that are provided in accordance with international statutory requirements. The Company accrues employee termination costs associated with an ongoing benefit arrangement if the obligation is attributed to prior services rendered, the rights to the benefits have vested and the payment is probable and the amount can be reasonably estimated. The Company accounts for employee termination benefits that represent a one-time benefit in accordance with FASB Statement No. 146, *Accounting for Costs Associated with Exit or Disposal Activities.* The Company generally records such costs into expense over the future service period, if any. In addition, in conjunction with an exit activity, the Company may offer voluntary termination benefits to employees. These benefits are recorded when the employee accepts the termination benefits and the amount can be reasonably estimated. Other costs associated with exit activities may include costs related to leased facilities to be abandoned or subleased and long-lived asset impairments.

During 2005, the Company recognized charges associated with exit activities of approximately $40 million. These charges included costs primarily attributable to employee terminations and outsourcing costs within the Company's human resources function and international divisions; and a $10 million write-off of intangible assets related to its Enteryx® Liquid Polymer Technology, a discontinued technology platform obtained as a part of its acquisition of Enteric Medical Technologies, Inc. (EMT). The write-off resulted from the Company's decision during the third quarter of 2005 to cease selling the Enteryx product.

Translation of Foreign Currency

The Company translates all assets and liabilities of foreign subsidiaries at the year-end exchange rate and translates sales and expenses at the average exchange rates in effect during the year. The net effect of these translation adjustments is shown in the accompanying financial statements as a component of stockholders' equity. Foreign currency transaction gains and losses are included in other, net in the consolidated statements of operations. These gains and losses were not material to the statements of operations for 2005, 2004, and 2003.

Financial Instruments

The Company recognizes all derivative financial instruments in the consolidated financial statements at fair value, regardless of the purpose or intent for holding the instrument, in accordance with FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*. Changes in the fair value of derivative instruments are recorded in earnings unless hedge accounting criteria are met. For derivative instruments designated as fair value hedges, the Company records the changes in fair value of both the derivative instrument and the hedged item in earnings. For derivative instruments designated as cash flow and net investment hedges, the effective portions of changes in fair value are recorded in other comprehensive income. The Company recognizes any ineffective portion of its hedges in earnings.

The carrying amounts of commercial paper and credit facility borrowings approximate their fair values. The fair value of the Company's fixed-rate long-term debt is based on market prices. Carrying amounts of floating-rate long-term debt approximate their fair value.

Shipping and Handling Costs

The Company does not generally bill customers for shipping and handling of its products. Shipping and handling costs of $92 million in 2005, $72 million in 2004 and $55 million in 2003 are included in selling, general and administrative expenses.

Research and Development

Research and development costs, including new product development programs, regulatory compliance and clinical research, are expensed as incurred.

Pension Plans

The Company maintains pension plans covering certain international employees, which the Company accounts for in accordance with FASB Statement No. 87, *Employers' Accounting for Pensions*. The assets, liabilities and costs associated with these plans were not material in 2005, 2004 and 2003.

Net Income Per Common Share

Net income per common share is based upon the weighted average number of common shares and common share equivalents outstanding each year.

New Accounting Standards

During 2004, the FASB issued Statement No. 123(R), *Share-Based Payment*, which is a revision of Statement No. 123, *Accounting for Stock-Based Compensation*. Statement No. 123(R) supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees* and amends Statement No. 95, *Statement of Cash Flows*. In general, Statement No. 123(R) contains similar accounting concepts as those described in Statement No. 123. However, Statement No. 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the consolidated statement of operations based on their fair values. Pro forma disclosure is no longer an alternative. Alternative phase-in methods are allowed under Statement No. 123(R). The Company adopted Statement No. 123(R) on its effective date of January 1, 2006 using the "modified-prospective method." Under this method, compensation cost is recognized (a) based on the requirements of Statement No. 123(R) for all share-based payments granted on or after January 1, 2006 and (b) based on the requirements of Statement No. 123 for all unvested awards that were granted to employees prior to January 1, 2006. The Company expects to apply the Black-Scholes valuation model in determining the fair value of share-based payments to employees, which will then be amortized on a straight-line basis.

As permitted by Statement No. 123, for periods prior to January 1, 2006, the Company accounted for share-based payments to employees using Opinion No. 25's intrinsic value method and, as such, generally recognized no compensation cost for the granting of employee stock options, except as disclosed in *Note L—Stock Ownership Plans*. Accordingly, the adoption of Statement No. 123(R)'s fair value method will negatively impact the Company's statements of operations. The impact of adoption of Statement No. 123(R) cannot be quantified at this time because it will depend on the level of share-based payments granted in the future, expected volatilities and expected useful lives, among other factors, present at the grant date. However, had Statement No. 123(R) been effective in prior periods, the impact of that standard would have approximated the impact of Statement No. 123 and net income and net income per share would have been reported as the following pro forma amounts:

(in millions, except per share data)	2005	2004	2003
Net income, as reported	$ 628	$1,062	$ 472
Add: Stock-based employee compensation expense included in net income, net of related tax effects	13	62	1
Less: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(74)	(67)	(62)
Pro forma net income	**$ 567**	**$1,057**	**$ 411**
Net income per common share			
Basic			
Reported	$0.76	$ 1.27	$0.57
Pro forma	$0.69	$ 1.26	$0.50
Assuming dilution			
Reported	$0.75	$ 1.24	$0.56
Pro forma	$0.68	$ 1.24	$0.49

Statement No. 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under currently effective accounting literature. This requirement will reduce net operating cash flows and increase net financing cash flows in periods after adoption of Statement No. 123(R). While the Company cannot estimate what those amounts will be in the future (because they depend on, among other things, when employees exercise stock options), the amount of operating cash flows recognized in prior periods for such excess tax deductions was $28 million in 2005, $185 million in 2004 and $154 million in 2003.

Further, most of the Company's stock option awards provide for immediate vesting upon retirement, death or disability of the participant. The Company has traditionally accounted for the pro forma compensation expense related to stock-based awards made to retirement eligible individuals using the stated vesting period of the grant. This approach results in compensation expense being recognized over the vesting period except in the instance of the participant's actual retirement. Statement No. 123(R) clarified the accounting for stock-based awards made to retirement eligible individuals, which explicitly provides that the vesting period for a grant made to a retirement eligible employee is considered non-substantive and should be ignored when determining the period over which the award should be expensed. Upon adoption of SFAS No. 123(R), the Company will be required to expense stock-based awards over the period between grant date and retirement eligibility or immediately if the employee is retirement eligible at the date of grant. If the Company had historically accounted for stock-based awards made to retirement eligible individuals under these requirements, the pro forma expense disclosed above would not have been materially impacted for the periods presented.

Reclassifications

The Company has reclassified certain prior year amounts to conform to the current year's presentation. See *Note N—Segment Reporting* for further details.

Note B – Other Balance Sheet Information

Components of selected captions in the consolidated balance sheets at December 31 are as follows:

(in millions)	2005	2004
Trade Accounts Receivable		
Accounts receivable	$1,015	$ 980
Less: allowances	83	80
	$ 932	**$ 900**
Inventories		
Finished goods	$ 286	$ 238
Work-in-process	64	65
Raw materials	68	57
	$ 418	**$ 360**
Property, Plant and Equipment		
Land	$ 76	$ 79
Buildings and improvements	625	588
Equipment, furniture and fixtures	1,152	978
	1,853	1,645
Less: accumulated depreciation	842	775
	$1,011	**$ 870**
Accrued Expenses		
Acquisition-related obligations	$ 357	$ 24
Payroll and related liabilities	294	255
Other	473	623
	$1,124	**$ 902**

Included in other accrued expenses at December 31, 2004 is a $110 million ($71 million after-tax) enhancement to the Company's 401(k) Retirement Savings Plan (401(k) Plan). On September 24, 2004, the Board of Directors approved an amendment to the Company's 401(k) Plan that provides for, among other things, a one-time enhancement to the 401(k) Plan. The Company apportioned this special retirement enhancement to eligible employees based on pay and years of service. The Company paid the one-time enhancement in the second quarter of 2005.

Included in other accrued expenses as of December 31, 2004 is a $75 million provision for a civil settlement with the Department of Justice. The Company paid the settlement in the second quarter of 2005.

In the second quarter of 2004, the company recorded inventory write-downs of $43 million (pre-tax) in conjunction with its recalls of certain units of the Company's TAXUS® Express²™ paclitaxel-eluting coronary stent systems and Express² coronary stent systems.

Note C – Investments in Strategic Alliances

The Company has entered a significant number of strategic alliances with privately held and publicly traded companies. Many of these alliances involve equity investments by the Company in privately held equity securities or investments where an observable quoted market value does not exist. The Company enters these strategic alliances to broaden its product technology portfolio and to strengthen and expand the Company's reach into existing and new markets. Many of these companies are in the developmental stage and have not yet commenced their principal operations. The Company's exposure to loss related to its strategic alliances is generally limited to its equity investments, notes receivable and intangible assets associated with these alliances.

Equity investments in strategic alliances at December 31 consist of the following:

	2005		2004	
(in millions)		Number of Strategic Investments		Number of Strategic Investments
Available-for-Sale Investments				
Amortized cost	$103		$ 76	
Gross unrealized gains	44		5	
Gross unrealized losses	(4)		(2)	
Fair value	$143	5	$ 79	3
Equity Method Investments				
Cost	$ 94		$ 64	
Equity in losses	(9)		(3)	
Carrying value	$ 85	3	$ 61	2
Cost Method Investments				
Carrying value	$366	58	$389	53
Total Investments	**$594**	**66**	**$529**	**58**

As of December 31, 2005, the Company held investments totaling $85 million in three companies that it accounted for under the equity method. The aggregate value of the Company's equity method investments for which a quoted market price is available is approximately $207 million, for which the associated carrying value is approximately $63 million. The Company's ownership percentages in these companies range from approximately 21 percent to 28 percent. The difference between the carrying value of these equity method investments and the value of the Company's share in the net assets of these investees is approximately $70 million. This difference is primarily attributable to goodwill and intangible assets subject to amortization, for which the estimated useful lives range from 10 to 20 years.

As of December 31, 2004, the Company held investments totaling $61 million in two companies that it accounted for under the equity method. The aggregate value of the Company's equity method investments for which a quoted market price was available was approximately $122 million, for which the associated carrying value was approximately $36 million. The Company's ownership percentages in these companies ranged from approximately 25 percent to 30 percent.

The Company regularly reviews its strategic investments for impairment indicators. Based on this review, the Company recorded other-than-temporary impairments of $10 million in 2005 associated with certain cost method investments. The remaining carrying value of these investments at December 31, 2005 was $16 million. The Company determined there were no impairment indicators present for the remaining $350 million of its cost method investments. The Company recorded other-than-temporary impairments of $3 million associated with certain of its available-for-sale investments. As of December 31, 2005, the Company had two available-for-sale investments with an aggregate carrying value of $10 million and unrealized loss position of $4 million. The duration of the unrealized loss position is less than 12 months. The Company does not consider these investments to be other-than-temporarily impaired at December 31, 2005 due to the duration of the impairment and the Company's ability and intent to hold the investment for a reasonable period of time sufficient for a forecasted recovery of the unrealized loss. In addition, during 2005, the Company wrote-off its $24 million investment in Medinol, Ltd. The Company's equity investment was canceled in conjunction with the litigation settlement with Medinol. The write-down of the Medinol investment is included in Litigation-related charges in the consolidated statements of operations.

The Company recorded other-than-temporary impairments of $45 million in 2004 associated with certain cost method investments. The remaining carrying value of these investments at December 31, 2004 was $27 million. The Company determined there were no impairment indicators present for $362 million of its cost method investments. As of December 31, 2004, the Company had one available-for-sale investment with a carrying value of $9 million in an unrealized loss position of $2 million. The duration of the unrealized loss position was less than 12 months. The Company did not consider this investment to be other-than-temporarily impaired at December 31, 2004 due to the duration of the impairment and the Company's ability and intent to hold the investment for a reasonable period of time sufficient for a forecasted recovery of the unrealized loss.

In 2005, the Company recorded realized gains of $4 million from sales of investments in privately held companies. In 2004, the Company recorded realized gains of $36 million from sales of investments in publicly traded and privately held companies.

The Company had approximately $112 million of notes receivable due from privately held and publicly traded companies at December 31, 2005, and $79 million of notes receivable at December 31, 2004. The Company recorded write-downs of notes receivable of $4 million in 2005 and $13 million in 2004.

Note D – Business Combinations

During 2005, the Company paid $178 million in cash to acquire TriVascular, Inc., CryoVascular Systems, Inc. and Rubicon Medical Corporation and paid $120 million in shares of the Company's common stock to acquire Advanced Stent Technologies, Inc. (AST). During 2004, the Company paid $804 million in cash to acquire Advanced Bionics Corporation and Precision Vascular Systems, Inc. (PVS). During 2003, the Company paid $13 million in cash to acquire InFlow Dynamics, Inc. These acquisitions were intended to strengthen the Company's leadership position in interventional medicine. The consolidated financial statements include the operating results for each acquired entity from its respective date of acquisition.

2005 Business Combinations

In March 2005, the Company acquired 100 percent of the fully diluted equity of AST for approximately 3.6 million shares of its own common stock, which was valued at approximately $120 million on the date of acquisition. The Company may also make earn-out payments in the future that are contingent upon AST achieving certain regulatory and performance-related milestones. AST is a developer of stent delivery systems that are designed to address coronary artery disease in bifurcated vessels. The acquisition was intended to provide the Company with an expanded stent technology and intellectual property portfolio.

In April 2005, the Company acquired 100 percent of the fully diluted equity of TriVascular for approximately $65 million in addition to its previous investments and notes issued of approximately $45 million. The Company may also make earn-out payments in the future that are contingent upon TriVascular achieving certain regulatory and performance-related milestones. TriVascular is a developer of medical devices and procedures used for treating abdominal aortic aneurysms (AAA). The acquisition was intended to expand the Company's vascular surgery technology portfolio.

In April 2005, the Company acquired 100 percent of the fully diluted equity of CryoVascular for approximately $50 million in addition to its previous investments of approximately $10 million. The Company may also make earn-out payments in the future that are contingent upon CryoVascular achieving certain performance related-milestones. CryoVascular is a developer and manufacturer of a proprietary angioplasty device to treat atherosclerotic disease of the legs and other peripheral arteries, which the Company previously distributed. The acquisition was intended to expand the Company's peripheral vascular technology portfolio.

In June 2005, the Company completed its acquisition of 100 percent of the fully diluted equity of Rubicon for approximately $70 million in addition to its previous investments of approximately $20 million. The Company may also make earn-out payments in the future that are contingent upon Rubicon achieving certain regulatory and performance related-milestones. Rubicon is a developer of embolic protection filters for use in interventional cardiovascular procedures. The acquisition was intended to strengthen the Company's leadership position in interventional cardiovascular procedures.

The Company allocated the excess of purchase price over the fair value of net tangible assets acquired to specific intangible asset categories for its 2005 acquisitions as follows:

(in millions)	Amount Assigned	Weighted Average Amortization Period	Risk-Adjusted Discount Rate used in Purchase Price Allocation
Amortizable Intangible Assets:			
Technology—core	$191	20 years	15%-24%
Technology—developed	59	10 years	15%
	$250	**18 years**	
Unamortizable Intangible Assets:			
Goodwill	$ 34		
Purchased research and development	$251		18%-27%

The Company recorded an aggregate deferred tax asset of $53 million and an aggregate deferred tax liability of $93 million in conjunction with the acquisitions completed during 2005. The deferred tax asset is primarily attributable to net operating loss carryforwards. The deferred tax liability mainly relates to the tax impact of future amortization associated with the identified intangible assets acquired in the acquisition.

2004 Business Combinations

On June 1, 2004, the Company completed its acquisition of 100 percent of the fully diluted equity of Advanced Bionics for an initial payment of approximately $740 million in cash, plus possible future earn-out payments. The initial purchase price was primarily funded by the issuance of commercial paper. Advanced Bionics develops implantable microelectronic technologies for treating numerous neurological disorders. Its neuromodulation technology includes a range of neurostimulators (or implantable pulse generators), programmable drug pumps and cochlear implants. At the acquisition date, Advanced Bionics had received FDA approval for certain auditory and pain management technologies. The auditory technology consists of a multichannel cochlear implant and an external sound processor that is capable of restoring the human sense of sound. The pain management technology consists of a spinal cord stimulation system for the treatment of chronic peripheral pain of the lower back and legs. In addition, Advanced Bionics had two significant projects in-process at the time of acquisition, including the bion® microstimulator and the drug delivery pump. The bion microstimulator is an implantable neurostimulation device designed to treat a variety of neurological conditions, including migraine headaches and urge incontinence. The drug delivery pump is an implanted programmable device designed to treat chronic pain. See the Purchased Research and Development section of this note for details on these two in-process projects. The Advanced Bionics acquisition was intended to expand the Company's technology portfolio into the implantable microelectronic device market.

The Advanced Bionics acquisition was structured to include earn-out payments that are primarily contingent on the achievement of future performance milestones. The performance milestones are segmented by Advanced Bionics' four principal technology platforms (cochlear implants, implantable pulse generators, drug pumps and bion microstimulators) and each milestone has a specific earn-out period, which generally commences on the date of the related product launch. Base earn-out payments on these performance milestones approximate two-and-a-quarter times incremental sales for each annual period. There are also bonus earn-out payments available based on the attainment of certain aggregate sales performance targets and a certain gross margin level. The milestones associated with the contingent consideration must be reached in certain periods through 2013. The estimated maximum potential amount of future contingent consideration (undiscounted) that the Company could be required to make associated with its acquisition of Advanced Bionics is approximately $2.4 billion. The estimated cumulative revenue level (undiscounted) associated with these maximum future contingent payments is approximately $5.6 billion during the period from 2006 through 2013. The Company will allocate these payments, if made, to goodwill.

Fair values of tangible assets and liabilities obtained in conjunction with the acquisition of Advanced Bionics were as follows:

(in millions)	
Assets	$64
Liabilities	35
Net Tangible Assets	**$29**

The Company allocated the excess of purchase price over the fair value of net tangible assets acquired to specific intangible asset categories as follows:

(in millions)	Amount Assigned	Weighted Average Amortization Period	Risk-Adjusted Discount Rate used in Purchase Price Allocation
Amortizable Intangible Assets:			
Technology—core	$325	20 years	17%-19%
Technology—developed	26	5 years	14%
Customer-related intangible assets	10	15 years	*
	$361	**19 years**	
Unamortizable Intangible Assets:			
Goodwill	$586		
Purchased research and development	$ 50		18%-27%

* The Company used the replacement cost method to value the customer-related intangible assets obtained in conjunction with the acquisition of Advanced Bionics.

The Advanced Bionics developed technology consists of auditory and pain management technologies that had received FDA approval as of the acquisition date. The Company determined that the estimated useful life of the developed technology was 5 years given the nature of microelectronic devices and the relatively rapid iteration of future generations of such technology.

The core technology consists of patented and unpatented fundamental neuromodulation platforms for auditory and pain management technologies. This core technology represents the common platform or the common parts within each of the acquired implantable microelectronic device technologies that will be carried over in future iterations of the product. The Company determined that the estimated useful life of the core technology was 20 years.

A significant excess of cost remained after allocating the purchase price to the net tangible and intangible assets, which the

Company allocated to goodwill. This significant amount of excess was attributable to the low level of net tangible assets acquired, the early stage of development of the acquired in-process technologies and the relatively short product life cycles of the developed technologies. The Company expected much of the value of the acquisition to be driven by future growth of the neuromodulation markets and technological developments impacting future product offerings. In addition, the goodwill encompasses the value associated with Advanced Bionics' highly technical and specialized assembled workforce; the value of synergies associated with the acquisition given Boston Scientifics' resources, including the Company's operational and global sales and marketing expertise; and the strategic benefit the Company expects to derive due to Advanced Bionics expanding its reach into the rapidly growing implantable microelectronic device market. The goodwill obtained in conjunction with the acquisition of Advanced Bionics is not deductible for tax purposes. The Company has allocated the goodwill to its reportable segments as follows: $468 million to the U.S., $71 million to Europe, $35 million to the Inter-Continental and $12 million to Japan. The Company allocated goodwill by business segment based on the respective revenue contribution during the year of acquisition.

The Company recorded a deferred tax asset of $85 million and a deferred tax liability of $134 million in conjunction with the acquisition of Advanced Bionics. The deferred tax asset is primarily attributable to net operating loss carryforwards. The deferred tax liability mainly relates to the tax impact of future amortization associated with the identified intangible assets acquired in the acquisition.

The following unaudited pro forma information presents the consolidated results of operations of the Company and Advanced Bionics as if the acquisition had occurred at the beginning of each of 2004 and 2003, with pro forma adjustments to give effect to amortization of intangible assets, an increase in interest expense on acquisition financing and certain other adjustments together with related tax effects:

(in millions, except per share data)	2004	2003
Net sales	$5,657	$3,532
Net income	1,079	425
Net income per share—basic	$ 1.29	$ 0.52
Net income per share—assuming dilution	$ 1.26	$ 0.50

The $50 million charge for purchased research and development that was a direct result of the transaction is excluded from the unaudited pro forma information above. The unaudited pro forma results are not necessarily indicative of the results that the Company would have attained had the acquisition of Advanced Bionics occurred at the beginning of the periods presented.

On April 2, 2004, the Company completed its acquisition of the remaining outstanding shares of PVS for an initial payment of approximately $75 million in cash. The Company may also make earn-out payments in the future that are contingent upon PVS achieving certain performance-related milestones. PVS develops and manufactures guidewires and microcatheter technology for use in accessing the brain, the heart and other areas of the anatomy. The acquisition of PVS was intended to provide the Company with additional vascular access technology.

2003 Business Combinations

On February 12, 2003, the Company completed its acquisition of InFlow. InFlow is a stent technology development company that focuses on reducing the rate of restenosis, improving the visibility of stents during procedures and enhancing the overall vascular compatibility of the stent. The acquisition was intended to provide the Company with an expanded stent technology and intellectual property portfolio.

The consolidated financial statements include the operating results for each acquired entity from its respective date of acquisition. Pro forma information is not presented for acquisitions other than Advanced Bionics, as the other acquired companies' results of operations prior to their date of acquisition are not material, individually or in the aggregate, to the Company.

Contingent Consideration

Certain of the Company's business combinations involve the payment of contingent consideration. For acquisitions completed before July 1, 2001, the Company allocates these payments, if made, to specific intangible asset categories, including purchased research and development, and assigns the remainder to goodwill as if it had paid the consideration at the date of acquisition. For acquisitions completed after June 30, 2001, the Company allocates these payments, if made, to related contingent consideration liabilities or goodwill. In accordance with Statement No. 142, the Company establishes a contingent consideration liability at the acquisition date if the sum of the fair value assigned to assets acquired (including purchased research and development) and liabilities assumed exceed the initial cost of the acquired entity. The liability established equals the lesser of the maximum amount of the potential contingent consideration or the excess fair value. Payment of the additional consideration is generally contingent upon the acquired companies' reaching certain performance milestones, including attaining specified

revenue levels, achieving product development targets or obtaining regulatory approvals.

During 2005, the Company paid $33 million for acquisition-related payments primarily associated with Catheter Innovations, Inc., Smart Therapeutics, Inc., and Embolic Protection, Inc. (EPI). As of December 31, 2005, the Company has recorded a liability of $89 million to account for the excess of the fair value of the assets acquired over the initial purchase price for certain of the Company's acquisitions. This liability will be reduced in conjunction with the future settlement of contingent consideration arrangements. In addition, as of December 31, 2005, the Company had accrued $268 million for acquisition-related payments, of which the Company paid approximately $210 million to Advanced Bionics during the first quarter of 2006. During 2004, the Company paid $107 million for acquisition-related payments primarily associated with EPI, Smart, and InFlow. In 2005 and 2004, the Company recorded amounts for acquisition-related obligations primarily as an adjustment to goodwill. During 2003, the Company paid $283 million for acquisition-related payments primarily associated with Interventional Technologies, Inc. (IVT), EMT and Smart. Of the amounts recorded for acquisition-related obligations in 2003, the Company recorded $24 million as an adjustment to purchased research and development, $9 million as an adjustment to other identifiable intangible asset categories, net of the related deferred tax liabilities, and the remainder as an adjustment to goodwill.

Certain earn-out payments are based on multiples of the acquired company's revenue during the earn-out period and, consequently, the Company cannot currently determine the total payments. However, the Company has developed an estimate of the maximum potential contingent consideration for each of its acquisitions with an outstanding earn-out obligation. At December 31, 2005, the estimated maximum potential amount of future contingent consideration (undiscounted) that the Company could be required to make associated with its business combinations is approximately $4 billion, some of which may be payable in common stock. The milestones associated with the contingent consideration must be reached in certain future periods ranging from 2006 through 2016. The estimated cumulative specified revenue level associated with these maximum future contingent payments is approximately $10 billion.

Purchased Research and Development

In 2005, the Company recorded $276 million of purchased research and development. The Company's 2005 purchased research and development consisted of: $130 million relating to the acquisition of TriVascular; $73 million relating to the acquisition of AST; $45 million relating to the acquisition of Rubicon; and $3 million relating to the acquisition of CryoVascular. In addition, the Company recorded $25 million of purchased research and development in conjunction with obtaining distribution rights for new brain monitoring technology that Aspect Medical Systems, one of the Company's strategic partners, is currently developing. This technology is designed to aid the diagnosis and treatment of depression, Alzheimer's disease and other neurological conditions.

The most significant 2005 purchased research and development projects included TriVascular's AAA stent-graft and AST's Petal™ bifurcation stent, which collectively represented 73 percent of the 2005 purchased research and development. TriVascular's AAA stent-graft design reduces the size of the stent-graft by replacing much of the metal stent assembly with a polymer that is injected into channels within the stent-graft during the procedure. During the fourth quarter of 2005, management decided to re-design certain aspects of the stent-graft to enhance patient safety and to improve product performance. The re-design will result in incremental costs and time to complete the project relative to those expected at the date of acquisition. The Company currently expects to launch the AAA stent-graft in the U.S. by 2011 and to incur approximately $200 million of research and development costs over the next five years to complete the project. The Company continues to assess the pace of development and its opportunities within this market, which may result in a delay in the timing of regulatory approval.

AST's Petal bifurcation stent is designed to expand into the side vessel when a single vessel branches into two vessels, permitting blood to flow into both branches of the bifurcation and providing support at the junction. The cost to complete the Petal bifurcation stent is estimated to be between $100 million and $125 million. As of the date the Company acquired AST, it expected the Petal bifurcation stent to be commercially available on a worldwide basis within six years in a drug-eluting configuration.

In 2004, the Company recorded $65 million of purchased research and development. The 2004 purchased research and development consisted primarily of $50 million relating to the acquisition of Advanced Bionics and $14 million relating to the acquisition of PVS. The most significant in-process projects acquired in connection with the Company's 2004 acquisitions included Advanced Bionics' bion microstimulator and drug delivery pump, which collectively represented 77 percent of the 2004 acquired in-process projects' value. The bion microstimulator is an implantable neurostimulation device designed to treat a variety of neurological conditions, including migraine headaches and urge

incontinence. The cost to complete the bion microstimulator is estimated to be between $35 million and $45 million. The Company expects that the bion microstimulator will be commercially available within three years. The Advanced Bionics drug delivery pump is an implanted programmable device designed to treat chronic pain. The cost to complete the drug delivery pump is estimated to be between $30 million and $40 million. The Company continues to assess the pace of development and its opportunities for the drug delivery pump, which may result in a delay in the timing of regulatory approval.

In 2003, the Company recorded $37 million of purchased research and development. The 2003 purchased research and development consisted of $9 million relating to the acquisition of InFlow and $28 million relating primarily to certain acquisitions that the Company consummated in prior years. The in-process projects acquired in connection with the acquisition of InFlow were not significant to the Company's consolidated results. The purchased research and development associated with the prior years' acquisitions related primarily to the 2001 acquisition of EPI and resulted from consideration that was contingent at the date of acquisition, but earned during 2003.

In connection with the Company's 2002 acquisitions, it acquired several in-process projects, including Smart's atherosclerosis stent. The atherosclerosis stent is a self-expanding nitinol stent designed to treat narrowing of the arteries around the brain. During 2005, the Company completed the atherosclerosis stent in-process project and received Humanitarian Device Exemption approval to begin selling this technology on a limited basis. The total cost for the Company to complete the project was approximately $10 million.

In connection with the Company's 2001 acquisitions, it acquired several significant in-process projects, including IVT's next-generation Cutting Balloon® device. The Cutting Balloon device is a novel balloon angioplasty device with mounted scalpels that relieve stress in the artery, reducing the force necessary to expand the vessel. During 2005, the Company completed the Cutting Balloon in-process project and received FDA approval for this technology. The total cost for the Company to complete the project was approximately $7 million.

Note E – Goodwill and Other Intangible Assets

The gross carrying amount of goodwill and intangible assets and the related accumulated amortization for intangible assets subject to amortization at December 31 are as follows:

(in millions)	2005 Gross Carrying Amount	2005 Accumulated Amortization	2004 Gross Carrying Amount	2004 Accumulated Amortization
Amortizable Intangible Assets				
Technology—core	$ 829	$ 86	$ 634	$ 48
Technology—developed	453	244	398	198
Patents	547	209	511	172
Other intangible assets	281	130	260	113
	$2,110	**$669**	**$1,803**	**$531**
Unamortizable Intangible Assets				
Goodwill	$1,938		$1,712	
Technology—core	356		356	
	$2,294		**$2,068**	

The Company's core technology that is not subject to amortization represents technical processes, intellectual property and/or institutional understanding acquired by the Company that is fundamental to the ongoing operation of the Company's business and has no limit to its useful life. The Company's core technology that is not subject to amortization is primarily comprised of certain purchased stent and balloon technology, which is foundational to the Company's continuing operation within the interventional cardiology market and other markets within interventional medicine. The Company amortizes all other core technology over its estimated useful life.

Estimated amortization expense for each of the five succeeding fiscal years based upon the Company's intangible asset portfolio at December 31, 2005 is as follows:

Fiscal Year	Estimated Amortization Expense (in millions)
2006	$135
2007	129
2008	111
2009	104
2010	90

Goodwill as of December 31 as allocated by segments of business is as follows:

(in millions)	United States	Europe	Japan	Inter-Continental
Balance as of December 31, 2003	$1,088	$115	$39	$33
Purchase price adjustments	(3)	(4)		
Goodwill acquired	320	48	8	24
Contingent consideration	35		8	
Foreign currency translation		1		
Balance as of December 31, 2004	$1,440	$160	$55	$57
Purchase price adjustments	(35)	(4)	(1)	(2)
Goodwill acquired	19	3	3	9
Contingent consideration	189	26	5	14
Balance as of December 31, 2005	**$1,613**	**$185**	**$62**	**$78**

The 2005 and 2004 purchase price adjustments relate primarily to adjustments to reflect properly the fair value of deferred tax assets and liabilities acquired in connection with current year and prior year acquisitions.

Note F – Borrowings and Credit Arrangements

The Company had outstanding borrowings of $2,020 million at December 31, 2005 at a weighted average interest rate of 4.80 percent as compared to outstanding borrowings of $2,367 million at December 31, 2004 at a weighted average interest rate of 3.38 percent.

Future debt obligations and the related interest payments as of December 31, 2005 are as follows:

	Payments Due by Period				
(in millions)	1 Year or less	2-3 Years	4-5 Years	After 5 Years	Total
Debt principal*	$156	$ 4	$ 2	$1,852	$2,014
Interest payments	100	200	200	846	1,346
Debt, including interest	**$256**	**$204**	**$202**	**$2,698**	**$3,360**

*Debt as reported in the Company's consolidated balance sheets includes the mark-to-market effect of its interest rate swaps and is net of the unamortized investor discount associated with the issuance of senior notes in conjunction with the Company's various public debt offerings.

Revolving Credit Facilities

During 2005, the Company refinanced its revolving credit facilities to extend the maturity of one credit facility and to reduce borrowing capacity by $165 million. At December 31, 2005, the Company's revolving credit facilities totaled approximately $2,020 million, as compared to $2,185 million at December 31, 2004. The Company's revolving credit facilities at December 31, 2005 consisted of a $1,500 million credit facility that terminates in May 2009; a $500 million credit facility that terminates in May 2010 and contains an option to increase the facility size by an additional $500 million in the future; and a $20 million uncommitted credit facility that terminates in May 2006. Use of the borrowings is unrestricted and the borrowings are unsecured.

The Company's credit facilities provide borrowing capacity and support its commercial paper program. The Company had $149 million of commercial paper outstanding at December 31, 2005 at a weighted average interest rate of 4.11 percent and $280 million outstanding at December 31, 2004 at a weighted average interest rate of 2.44 percent. In September 2005, the Company repaid 45 billion Japanese yen (approximately $400 million) in credit facility borrowings outstanding at a weighted average interest rate of 0.37 percent.

During 2005, the Company decreased its credit and security facility that is secured by its U.S. trade receivables from $400 million to $100 million, effective April 30, 2005. During the first quarter of 2006, the Company expects to increase this facility from $100 million to $350 million. The credit and security facility terminates in August 2006. Borrowing availability under this facility changes based upon the amount of eligible receivables, concentration of eligible receivables and other factors. Certain significant changes in the quality of the Company's receivables may require it to repay borrowings immediately under the facility. The credit agreement required the Company to create a wholly-owned entity, which is consolidated. This entity purchases the Company's U.S. trade accounts receivable and then borrows from two third-party financial institutions using these receivables as collateral. The receivables and related borrowings remain on the balance sheet because the Company has the right to prepay any borrowings outstanding and effectively retain control over the receivables. Accordingly, pledged receivables are included as trade accounts receivable, net, while the corresponding borrowings are included as debt on the consolidated balance sheets. There were no outstanding borrowings under the revolving credit and security facility as of December 31, 2005 or December 31, 2004.

In addition, the Company has uncommitted credit facilities with two commercial Japanese banks that provide for borrowings and promissory notes discounting of up to 15 billion Japanese yen (translated to $127 million at December 31, 2005 and $145 million at December 31, 2004). Approximately $109 million of notes receivable were discounted at an average interest rate of 0.75 percent at December 31, 2005 and $128 million of notes receivable were discounted at an average interest rate of 0.75 percent at December 31, 2004.

As of December 31, 2005 and December 31, 2004, the Company intends to repay all of its short-term debt obligations within the next twelve-month period.

Senior Notes

The Company had senior notes of $1,850 million outstanding at December 31, 2005 and $1,600 million outstanding at December 31, 2004.

- In November 2005, the Company issued $400 million of senior notes due November 2015 (November 2015 Notes) and $350 million of senior notes due November 2035 (November 2035 Notes) under a $1,500 million shelf registration statement filed with the SEC in November 2004. The November 2015 Notes bear a semi-annual coupon of 5.50 percent, are redeemable prior to maturity and are not subject to any sinking fund requirements. The November 2035 Notes bear a semi-annual coupon of 6.25 percent, are redeemable prior to maturity and are not subject to any sinking fund requirements. These are publicly registered securities. In December 2005, the Company announced its intent to supplement the terms of the Company's November 2015 Notes and November 2035 Notes to provide for a potential interest rate adjustment accruing from November 17, 2005 on each series of these senior notes in the event that the Company's credit ratings are downgraded as a result of the closing of its proposed acquisition of Guidant Corporation. The interest rate on these senior notes will be subject to a one-time increase based on the Company's initial credit ratings. Based on preliminary indications from the rating agencies, the Company expects that the interest rate on each of its November 2015 Notes and its November 2035 Notes may increase by 0.75 percent. The Company will be unable to determine the actual increase, if any, of the interest rate on each of the November 2015 Notes and November 2035 Notes until after the closing of the Company's proposed acquisition of Guidant. Any subsequent rating improvements will result in a decrease in the adjusted interest rate. The interest rate on the date these senior notes were originally issued will be permanently reinstated if and when the lowest credit ratings assigned to these senior notes is either A- or A3 or higher.
- In March 2005, the Company repaid $500 million of senior notes which were outstanding at December 31, 2004. The notes bore a semi-annual coupon of 6.625 percent, were not redeemable prior to maturity and were not subject to any sinking fund requirements.
- In November 2004, the Company issued $250 million of senior notes due January 2011 (January 2011 Notes) and $250 million of senior notes due January 2017 (January 2017 Notes) under a shelf registration statement filed with the SEC in November 2004. The January 2011 Notes bear a semi-annual coupon of 4.25 percent, are redeemable prior to maturity and are not subject to any sinking fund requirements. The January 2017 Notes bear a semi-annual coupon of 5.125 percent, are redeemable prior to maturity and are not subject to any sinking fund requirements. These senior notes are publicly registered securities. The Company entered into fixed-to-floating interest rate swaps indexed to six-month LIBOR, which approximated 4.70 percent at December 31, 2005 and 2.78 percent at December 31, 2004, to hedge against changes in the fair value of these senior notes.
- In June 2004, the Company issued $600 million of senior notes due June 2014 (June 2014 Notes) under a shelf registration statement filed with the SEC. The June 2014 Notes bear a semi-annual coupon of 5.45 percent, are redeemable prior to maturity and are not subject to any sinking fund requirements. These senior notes are publicly registered securities. The Company entered into fixed-to-floating interest rate swaps indexed to six-month LIBOR, which approximated 4.70 percent at December 31, 2005 and 2.78 percent at December 31, 2004, to hedge against changes in the fair value of these senior notes.

See *Note G—Financial Instruments* for further discussion regarding the treatment of the Company's interest rate swaps.

The remainder of the Company's outstanding borrowings, including capital lease arrangements, was immaterial at December 31, 2005 and December 31, 2004.

Note G – Financial Instruments

Carrying amounts and fair values of the Company's financial instruments at December 31 are as follows:

	2005		2004	
(in millions)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets				
Foreign exchange contracts	$ 176	$ 176	$ 70	$ 70
Interest rate swap contracts	21	21	32	32
Liabilities				
Long-term debt—fixed-rate	$1,862	$1,859	$1,135	$1,140
Foreign exchange contracts	55	55	129	129
Interest rate swap contracts	7	7	1	1

Considerable judgment is required in interpreting market data to develop estimates of fair value. Estimates presented herein are not necessarily indicative of the amounts that the Company could realize in a current market exchange due to changes in market rates since the reporting date.

Derivative Instruments and Hedging Activities

The Company develops, manufactures and sells medical devices globally and its earnings and cash flows are exposed to market risk from changes in currency exchange rates and interest rates. The Company addresses these risks through a risk management program that includes the use of derivative financial instruments. The Company operates the program pursuant to documented corporate risk management policies. The Company does not enter into derivative transactions for speculative purposes.

The Company estimates the fair value of derivative financial instruments based on the amount that it would receive or pay to terminate the agreements at the reporting date. The Company had currency derivative instruments outstanding in the contract amounts of $3,593 million at December 31, 2005 and $4,171 million at December 31, 2004. The decrease in the outstanding amount of the Company's currency derivative instruments is primarily due to the maturity of hedge contracts. In addition, the Company had interest rate swap contracts outstanding in the notional amounts of $1,100 million at December 31, 2005 and $1,600 million at December 31, 2004. The decrease in the notional amount of the Company's interest rate swaps is due to the maturing of hedge contracts related to the Company's $500 million 6.625 percent senior notes, which were repaid upon maturity during March 2005.

Currency Transaction Hedging

The Company manages its currency transaction exposures on a consolidated basis to take advantage of offsetting transactions. The Company uses foreign currency denominated borrowings and currency forward contracts to manage the majority of the remaining transaction exposure. These currency forward contracts are not designated as cash flow, fair value or net investment hedges under Statement No. 133; are marked-to-market with changes in fair value recorded to earnings; and are entered into for periods consistent with currency transaction exposures, generally one to six months. These derivative instruments do not subject the Company's earnings or cash flows to material risk since gains and losses on these derivatives generally offset losses and gains on the assets and liabilities being hedged. Changes in currency exchange rates related to any unhedged transactions may impact the Company's earnings and cash flows.

Currency Translation Hedging

The Company uses currency forward and option contracts to reduce the risk that the Company's earnings and cash flows, associated with forecasted foreign currency denominated intercompany and third-party transactions, will be affected by currency exchange rate changes. Changes in currency exchange rates related to any unhedged transactions may impact the Company's earnings and cash flows. The success of the hedging program depends, in part, on forecasts of transaction activity in various currencies (primarily Japanese yen, euro, British pound sterling, Australian dollar and Canadian dollar). The Company may experience unanticipated currency exchange gains or losses to the extent that there are timing differences between forecasted and actual activity during periods of currency volatility. The effective portion of any change in the fair value of the derivative instruments, designated as cash flow hedges, is recorded in other comprehensive income until the related third-party transaction occurs. Once the related third-party transaction occurs, the Company reclassifies the effective portion of any related gain or loss on the cash flow hedge from other comprehensive income to earnings. In the event the hedged forecasted transaction does not occur, or it becomes probable that it will not occur, the Company would reclassify the effective portion of any gain or loss on the related cash flow hedge from other comprehensive income to earnings at that time. The Company did not recognize material gains or losses resulting from hedge ineffectiveness during 2005, 2004, or 2003. The Company recognized a net loss of $12 million during 2005, $51 million during 2004, and $8 million during 2003 on hedge contracts that matured in accordance with the Company's currency translation risk management program. All cash flow hedges outstanding at December 31, 2005 mature within the subsequent 36-month period. As of December 31, 2005, $67 million of net unrealized gains are recorded in accumulated

other comprehensive income, net of tax, to recognize the effective portion of any fair value of derivative instruments that are, or previously were, designated as cash flow hedges as compared to $51 million of net unrealized losses at December 31, 2004. At December 31, 2005, $41 million of net gains, net of tax, may be reclassified to earnings within the next twelve-months to mitigate foreign exchange risk.

Interest Rate Hedging

The Company uses interest rate derivative instruments to manage its exposure to interest rate movements and to reduce borrowing costs by converting floating-rate debt into fixed-rate debt or fixed-rate debt into floating-rate debt. These derivative instruments are designated as either fair value or cash flow hedges under Statement No. 133. The Company records changes in the fair value of fair value hedges in other income and expense, which is offset by changes in the fair value of the hedged debt obligation to the extent the hedge is effective. Interest expense reflects interest payments made or received under interest rate derivative instruments. The Company records any change in the fair value of cash flow hedges as other comprehensive income, net of tax, and reclassifies the fair value to interest expense during the hedged interest payment period.

To hedge against potential changes in the fair value of certain of its senior notes, the Company entered into fixed-to-floating interest rate swaps indexed to six-month LIBOR, which approximated 4.70 percent at December 31, 2005 and 2.78 percent at December 31, 2004. These interest rate swaps are designated as fair value hedges and as such, the Company has recorded changes in the fair value of its hedged senior notes since entering the interest rate swaps. As of December 31, 2005, the carrying amount of certain of the Company's senior notes included $21 million of unrealized gains that the Company recorded as other long-term assets and $7 million of unrealized losses recorded as other long-term liabilities to recognize the fair value of the interest rate swaps. As of December 31, 2004, the carrying amount of certain of the Company's senior notes included $32 million of unrealized gains that the Company recorded as other long-term assets and $1 million of unrealized losses recorded as other long-term liabilities to recognize the fair value of the interest rate swaps. The Company recognized $9 million of interest expense reductions related to interest rate derivative contracts in 2005 as compared to $16 million in 2004 and $7 million in 2003.

Note H – Leases

Rent expense amounted to $63 million in 2005, $50 million in 2004 and $48 million in 2003. Future minimum rental commitments at December 31, 2005 under noncancelable operating lease agreements are as follows:

(in millions)	Operating Leases
2006	$ 47
2007	34
2008	22
2009	6
2010	3
Thereafter	2
Total minimum lease payments	**$114**

The Company's obligations under noncancelable capital leases were immaterial as of December 31, 2005 and December 31, 2004.

Note I – Income Taxes

Income before income taxes consists of the following:

(in millions)	2005	2004	2003
Domestic	$ (126)	$ 353	$231
Foreign	1,017	1,141	412
	$ 891	**$1,494**	**$643**

The related provision for income taxes consists of the following:

(in millions)	2005	2004	2003
Current			
Federal	$153	$245	$159
State	37	20	7
Foreign	69	137	36
	$259	**$402**	**$202**
Deferred			
Federal	$ (25)	$ 73	$ (27)
State	(1)	4	(1)
Foreign	30	(47)	(3)
	4	**30**	**(31)**
	$263	**$432**	**$171**

The reconciliation of income taxes at the federal statutory rate to the actual provision for income taxes is as follows:

	2005	2004	2003
U.S. federal statutory income tax rate	35.0%	35.0%	35.0%
State income taxes, net of federal benefit	3.0%	1.1%	0.6%
Effect of foreign taxes	(34.3)%	(13.5)%	(8.8)%
Non-deductible merger expenses	9.9%	1.5%	2.0%
Research credit	(1.6)%	(1.4)%	(1.6)%
Legal settlement	10.2%	1.8%	
Extraordinary dividend from subsidiaries	(0.7)%	4.1%	
Sale of intangible assets	5.9%		
Other, net	2.1%	0.3%	(0.6)%
	29.5%	**28.9%**	**26.6%**

Significant components of the Company's deferred tax assets and liabilities at December 31 are as follows:

(in millions)	2005	2004
Deferred Tax Assets		
Inventory costs, intercompany profit and related reserves	$ 142	$175
Tax benefit of net operating loss, capital loss and tax credits	154	170
Reserves and accruals	125	145
Restructuring and merger-related charges, including purchased research and development	144	161
Unrealized losses on derivative financial instruments		30
Other	53	60
	618	741
Less: valuation allowance on deferred tax assets	17	23
	$ 601	**$718**
Deferred Tax Liabilities		
Property, plant and equipment	$ 10	$ 19
Intangible assets	453	432
Unremitted earnings of subsidiaries	133	233
Litigation settlement	24	23
Unrealized gains on available-for-sale securities	14	1
Unrealized gains on derivative financial instruments	39	
Other	38	28
	711	**736**
	$(110)	**$ (18)**

During the first quarter of 2005, the Company repatriated approximately $1,046 million in extraordinary dividends as defined in the American Jobs Creation Act from its non-U.S. operations. The American Jobs Creation Act, enacted in October 2004, created a temporary incentive for U.S. corporations to repatriate accumulated income earned abroad by providing an 85 percent dividends received deduction for certain dividends from controlled foreign corporations. As of December 31, 2004, the Company recorded a tax liability of $61 million for the amounts it intended to repatriate in 2005 under the American Jobs Creation Act. In the first quarter of 2005, the Company adjusted the deferred tax liability that it had established at December 31, 2004 by $6 million for a technical correction made to the American Jobs Creation Act.

In 2005, the Company repatriated earnings of non-U.S. subsidiaries for which it had previously accrued tax liabilities. The resulting tax liabilities associated with this repatriation were $127 million. In addition, during 2005, the Company made a decision to repatriate additional amounts from certain of its non-U.S. operations. In connection with this decision, the Company established a deferred tax liability of $27 million that it believes is adequate to cover the taxes related to this repatriation. The tax liability the Company accrued for earnings of non-U.S. subsidiaries to be remitted in the future is $133 million at December 31, 2005.

At December 31, 2005, the Company had U.S. tax net operating loss, capital loss and tax credit carryforwards, the tax effect of which is $103 million. In addition, the Company had foreign tax net operating loss carryforwards, the tax effect of which is $51 million. These carryforwards will expire periodically beginning in 2006. The Company established a valuation allowance of $17 million against these carryforwards. The decrease in the valuation allowance from 2004 to 2005 is primarily attributable to utilization of foreign tax credits and foreign net operating losses reserved for in prior years.

The income tax provision of the unrealized gain or loss component of other comprehensive income was $82 million in 2005, $30 million in 2004 and $5 million in 2003.

Note J – Commitments and Contingencies

The interventional medicine market in which the Company primarily participates is in large part technology driven. Physician customers, particularly in interventional cardiology, move quickly to new products and new technologies. As a result, intellectual property rights, particularly patents and trade secrets, play a significant role in product development and differentiation. However, intellectual property litigation to defend or create market advantage is inherently complex and unpredictable. Furthermore, appellate courts frequently overturn lower court patent decisions.

In addition, competing parties frequently file multiple suits to leverage patent portfolios across product lines, technologies and geographies and to balance risk and exposure between the parties. In some cases, several competitors are parties in the same proceeding, or in a series of related proceedings, or litigate multiple features of a single class of devices. These forces frequently drive settlement not only of individual cases, but also of a series of pending and potentially related and unrelated cases. In addition, although monetary and injunctive relief is typically sought, remedies and restitution are generally not determined until the conclusion of the proceedings and are frequently modi-

fied on appeal. Accordingly, the outcomes of individual cases are difficult to time, predict or quantify and are often dependent upon the outcomes of other cases in other geographies.

Several third parties have asserted that the Company's current and former stent systems infringe patents owned or licensed by them. The Company has similarly asserted that stent systems or other products sold by these companies infringe patents owned or licensed by the Company. Adverse outcomes in one or more of the proceedings against the Company could limit the Company's ability to sell certain stent products in certain jurisdictions, or reduce its operating margin on the sale of these products. In addition, damage awards related to historical sales could be material.

In management's opinion, the Company is not currently involved in any legal proceeding other than those specifically identified below, which, individually or in the aggregate, could have a material effect on its financial condition, operations and/or cash flows. Unless otherwise indicated below, a range of loss associated with any individual material legal proceeding can not be estimated.

Litigation with Johnson & Johnson

On October 22, 1997, Cordis Corporation, a subsidiary of Johnson & Johnson, filed a suit for patent infringement against the Company and SCIMED Life Systems, Inc., a subsidiary of the Company, alleging that the importation and use of the NIR® stent infringes two patents owned by Cordis. On April 13, 1998, Cordis filed a suit for patent infringement against the Company and SCIMED alleging that the Company's NIR® stent infringes two additional patents owned by Cordis. The suits were filed in the U.S. District Court for the District of Delaware seeking monetary damages, injunctive relief and that the patents be adjudged valid, enforceable and infringed. A trial on both actions was held in late 2000. A jury found that the NIR® stent does not infringe three Cordis patents, but does infringe one claim of one Cordis patent and awarded damages of approximately $324 million to Cordis. On March 28, 2002, the Court set aside the damage award, but upheld the remainder of the verdict, and held that two of the four patents had been obtained through inequitable conduct in the U.S. Patent and Trademark Office. On May 16, 2002, the Court also set aside the verdict of infringement, requiring a new trial. On March 24, 2005, in a second trial, a jury found that a single claim of the Cordis patent was valid and infringed. The jury determined liability only; any monetary damages will be determined at a later trial. The Company, however, has requested the judge to enter judgment in its favor as a matter of law, and intends to appeal any adverse decision. Even though it is reasonably possible that the Company may incur a liability associated with this case, the Company does not believe that a loss is probable or estimable. Therefore, the Company has not accrued for any losses associated with this case.

On March 21, 1997, the Company (through its subsidiaries) filed a suit against Johnson & Johnson (through its subsidiaries) in Italy seeking a declaration of noninfringement for the NIR® stent relative to one of the European patents licensed to Ethicon, Inc. (Ethicon), a subsidiary of Johnson & Johnson, and a declaration of invalidity. A technical expert was appointed by the Court and a hearing was held on January 30, 2002. A decision was rendered on September 16, 2004, finding the NIR® stent does not infringe the European patent licensed to Ethicon. A decision with respect to invalidity has not yet been issued.

On April 2, 1997, Ethicon and other Johnson & Johnson subsidiaries filed a cross-border proceeding in The Netherlands alleging that the NIR® stent infringes a European patent licensed to Ethicon. In this action, the Johnson & Johnson entities requested relief, including provisional relief (a preliminary injunction). In October 1997, Johnson & Johnson's request for provisional cross-border relief on the patent was denied by the Dutch Court, on the ground that it is "very likely" that the NIR® stent will be found not to infringe the patent. Johnson & Johnson's appeal of this decision was denied. In January 1999, Johnson & Johnson amended the claims of the patent and changed the action from a cross-border case to a Dutch national action. On June 23, 1999, the Dutch Court affirmed that there were no remaining infringement claims with respect to the patent and also asked the Dutch Patent Office for technical advice about the validity of the amended patent. In late 1999, Johnson & Johnson appealed this decision. On March 11, 2004, the Court of Appeals nullified the Dutch Court's June 23, 1999 decision and the proceedings have been returned to the Dutch Court. In accordance with its 1999 decision, the Dutch Court asked the Dutch Patent Office for technical advice on the validity of the amended patent. On August 31, 2005, the Dutch Patent Office issued its technical advice that the amended patent was valid but left certain legal issues for the Dutch Court to resolve. At this time, no further proceedings have occurred in the Dutch Court.

On August 22, 1997, Johnson & Johnson filed a suit for patent infringement against the Company alleging that the sale of the NIR® stent infringes certain Canadian patents owned by Johnson & Johnson. Suit was filed in the federal court of Canada seeking a declaration of infringement, monetary damages and injunctive relief. On December 2, 2004, the Court dismissed the case, finding all patents to be invalid. On December 6, 2004,

Johnson & Johnson appealed the Court's decision. A hearing on the appeal has not yet been scheduled.

On March 30, 2000, the Company (through its subsidiary) filed suit for patent infringement against two subsidiaries of Cordis alleging that Cordis' Bx Velocity® stent delivery system infringes a published utility model owned by Medinol and exclusively licensed to the Company. The complaint was filed in the District Court of Dusseldorf, Germany seeking monetary and injunctive relief. A hearing was held on March 15, 2001, and on June 6, 2001, the Court issued a written decision that Cordis' Bx Velocity stent delivery system infringes the Medinol published utility model. Cordis appealed the decision of the German court. A hearing on the appeal originally scheduled for April 3, 2003 was suspended until decisions were rendered in two actions pending in the U.S. District Court of New York between Medinol and the Company. On October 19, 2004, Medinol filed an Intervention action requesting that the Court declare that the Company is not entitled to bring the infringement claim against Cordis and to declare that Cordis infringes the Medinol utility model. As a result of the Company's settlement with Medinol in September 2005, the Company assigned all of its rights to bring the suit and rights to damages to Medinol.

On February 14, 2002, the Company and certain of its subsidiaries filed suit for patent infringement against Johnson & Johnson and Cordis alleging that certain balloon catheters and stent delivery systems sold by Johnson & Johnson and Cordis infringe five U.S. patents owned by the Company. The complaint was filed in the U.S. District Court for the Northern District of California seeking monetary and injunctive relief. On October 15, 2002, Cordis filed a counterclaim alleging that certain balloon catheters and stent delivery systems sold by the Company infringe three U.S. patents owned by Cordis and seeking monetary and injunctive relief. On December 6, 2002, the Company filed an amended complaint alleging that two additional patents owned by the Company are infringed by the Cordis products. A bench trial on interfering patent issues was held December 5, 2005 and the filing of post trial briefs is in process. A trial on infringement has not yet been scheduled.

On March 26, 2002, the Company and Target Therapeutics, Inc., a wholly owned subsidiary of the Company, filed suit for patent infringement against Cordis alleging that certain detachable coil delivery systems and /or pushable coil vascular occlusion systems (coil delivery systems) infringe three U.S. patents, owned by or exclusively licensed to Target. The complaint was filed in the U.S. District Court for the Northern District of California seeking monetary and injunctive relief. A summary judgment hearing was held on April 19, 2004, and on June 25, 2004, the Court granted summary judgment in favor of the Company finding infringement of one of the patents. On February 3, 2005, the Court granted a stay in the proceedings pending reexamination of two of the patents by the U.S. Patent and Trademark Office. Summary judgment motions on the validity of the remaining patent are pending with one hearing held on September 26, 2005, and another held on November 14, 2005. On November 14, 2005, the Court denied Cordis' summary judgment motions with respect to the validity of the patent. A trial is expected to begin on September 12, 2006.

On January 13, 2003, Cordis filed suit for patent infringement against the Company and SCIMED alleging the Company's Express²™ coronary stent infringes a U.S. patent owned by Cordis. The suit was filed in the U.S. District Court for the District of Delaware seeking monetary and injunctive relief. On August 4, 2004, the Court granted a Cordis motion to add the Company's Liberté™ coronary stent and two additional patents to the complaint. On June 21, 2005, a jury found that the Company's TAXUS® Express²™, Express², Express™ Biliary, and Liberté stents infringe a Johnson & Johnson patent and that the Liberté stent infringes a second Johnson & Johnson patent. The juries only determined liability; monetary damages will be determined at a later trial. The Company has requested the judge to enter judgment in its favor as a matter of law. The Company intends to appeal any adverse decision. Even though it is reasonably possible that the Company may incur a liability associated with this case, the Company does not believe that a loss is probable or estimable. Therefore, the Company has not accrued for any losses associated with this case. On July 1, 2005, a jury found that Johnson & Johnson's Cypher®, Bx Velocity®, Bx Sonic™ and Genesis™ stents infringe the patent in the Company's counterclaim.

On March 13, 2003, the Company and Boston Scientific Scimed, Inc. filed suit for patent infringement against Johnson & Johnson and Cordis, alleging that its Cypher drug-eluting stent infringes a patent owned by the Company. The suit was filed in the District Court of Delaware seeking monetary and injunctive relief. Cordis answered the complaint, denying the allegations, and filed a counterclaim against the Company alleging that the patent is not valid and is unenforceable. The Company subsequently filed amended and new complaints in the District Court of Delaware alleging that the Cypher drug-eluting stent infringes four additional patents owned by the Company. Following the announcement on February 23, 2004 by Guidant Corporation of an agreement with Johnson & Johnson and Cordis to sell the Cypher drug-eluting stent, the Company amended its complaint to include Guidant and

certain of its subsidiaries as co-defendants as to certain patents in suit. In March 2005, the Company filed a stipulated dismissal as to three of the patents. On July 1, 2005, a jury found that Johnson & Johnson's Cypher drug-eluting stent infringes one of the Company's patents. The jury upheld the validity of the patent. The jury determined liability only; any monetary damages will be determined at a later trial. Johnson & Johnson has requested the judge to enter judgment in its favor as a matter of law. The trial on the second remaining patent against Johnson & Johnson, Cordis and Guidant has been postponed.

On December 24, 2003, the Company (through its subsidiary Schneider Europe GmbH) filed suit against the Belgian subsidiaries of Johnson & Johnson, Cordis and Janssen Pharmaceutica alleging that Cordis' Bx Velocity stent, Bx Sonic® stent, Cypher stent, Cypher Select stent, Aqua T3™ balloon and U-Pass balloon infringe one of the Company's European patents. The suit was filed in the District Court of Brussels, Belgium seeking preliminary cross-border, injunctive and monetary relief and sought an expedited review of the claims by the Court. A separate suit was filed in the District Court of Brussels, Belgium against nine additional Johnson & Johnson subsidiaries. On February 9, 2004, the Belgium Court linked all Johnson & Johnson entities into a single action. A hearing was held on June 7, 2004, and on June 21, 2004, the Court dismissed the case for failure to satisfy the requirements for expedited review without commenting on the merits of the claims. On August 5, 2004, the Company refiled the suit on the merits against the same Johnson & Johnson subsidiaries in the District Court of Brussels, Belgium seeking cross-border, injunctive and monetary relief for infringement of the same European patent. A hearing date has not yet been set. In December 2005, the Johnson & Johnson subsidiaries filed a nullity action in France and, in January 2006, the same Johnson & Johnson subsidiaries filed nullity actions in Italy and Germany.

On May 12, 2004, the Company (through its subsidiary Schneider Europe GmbH) filed suit against two of Johnson & Johnson's Dutch subsidiaries, alleging that Cordis' Bx Velocity stent, Bx Sonic stent, Cypher stent, Cypher Select stent, and Aqua T3 balloon delivery systems for those stents, and U-Pass angioplasty balloon catheters infringe one of the Company's European patents. The suit was filed in the District Court of The Hague in The Netherlands seeking injunctive and monetary relief. On June 8, 2005, the Court found the Johnson & Johnson products infringe the Company's patent and granted injunctive relief. On June 23, 2005, the District Court in Assen, The Netherlands stayed enforcement of the injunction. On October 12, 2005, a Dutch Court of Appeals overturned the Assen court's ruling and reinstated the injunction against the manufacture, use and sale of the Cordis products in the Netherlands. Damages for Cordis' infringing acts in the Netherlands will be determined at a later date. Cordis' appeal of the validity and infringement ruling by The Hague court remains pending.

On September 27, 2004, Boston Scientific Scimed, Inc. filed suit against a German subsidiary of Johnson & Johnson alleging the Cypher drug-eluting stent infringes a European patent owned by the Company. The suit was filed in Mannheim, Germany seeking monetary and injunctive relief. A hearing was held on April 1, 2005 and on July 15, 2005, the Court indicated that it would appoint a technical expert. A final hearing has not yet been scheduled.

On October 15, 2004, Boston Scientific Scimed, Inc. filed suit against a German subsidiary of Johnson & Johnson alleging the Cypher drug-eluting stent infringes a German utility model owned by the Company. The suit was filed in Mannheim, Germany seeking monetary and injunctive relief. A hearing was held on April 1, 2005 and on July 15, 2005, the Court indicated that it would appoint a technical expert. A final hearing has not yet been scheduled.

On December 30, 2004, Boston Scientific Scimed, Inc. (Scimed), a wholly-owned subsidiary of the Company, filed suit against a German subsidiary of Johnson & Johnson alleging the Cypher drug-eluting stent infringes a German utility model owned by the Company. The suit was filed in Dusseldorf, Germany seeking monetary and injunctive relief. A hearing was held on December 1, 2005. In January 2006, the judge rendered a decision of non-infringement. On January 29, 2006, Scimed appealed the judge's decision.

Litigation with Guidant Corporation

On December 18, 2004, the Company and SCIMED filed suit for patent infringement against Guidant and certain of its subsidiaries alleging that Guidant's ACCULINK™ stent and ACCUNET™ embolic protection system infringes three U.S. patents owned by the Company. The complaint was filed in the U.S. District Court for the District of Minnesota seeking monetary and injunctive relief. On January 26, 2005, Guidant answered the complaint. Trial is expected to begin in January 2007.

Litigation with Medtronic, Inc.

On August 13, 1998, Medtronic AVE, Inc., a subsidiary of Medtronic, Inc., filed a suit for patent infringement against the Company and SCIMED alleging that the Company's NIR® stent infringes two patents owned by Medtronic AVE. The suit was

filed in the U.S. District Court for the District of Delaware seeking injunctive and monetary relief. On May 25, 2000, Medtronic AVE amended the complaint to include a third patent. Cross-motions for summary judgment were filed and hearings were held on October 21 and 22, 2004. On January 5, 2005, the Court found the NIR® stent not to infringe the patents and on February 2, 2005, issued final judgment in favor of the Company. Medtronic appealed the judgment on March 16, 2005. A hearing on the appeal has been scheduled for April 5, 2006.

On January 15, 2004, Medtronic Vascular, Inc., a subsidiary of Medtronic, filed suit against the Company and SCIMED alleging the Company's Express® coronary stent and Express²™ coronary stent infringe four U.S. patents owned by Medtronic Vascular. The suit was filed in the District Court of Delaware seeking monetary and injunctive relief. Cross-motions for summary judgment were filed and hearings were held on October 21 and 22, 2004. On January 5, 2005, the Court found the Express coronary stent and Express² coronary stent not to infringe the patents and on February 2, 2005, issued final judgment in favor of the Company. Medtronic appealed the judgment on March 16, 2005. A hearing on the appeal has been scheduled for April 5, 2006.

Litigation Relating to Advanced Neuromodulation Systems, Inc.

On April 21, 2004, Advanced Neuromodulation Systems, Inc. (ANSI) filed suit against Advanced Bionics, a subsidiary of the Company, alleging that its Precision® spinal cord stimulation system infringes a U.S. patent owned by ANSI. The suit also included allegations of misappropriation of trade secrets and tortious interference with a contract. The suit was filed in the U.S. District Court for the Eastern District of Texas seeking monetary and injunctive relief. On August 6, 2004, Advanced Bionics moved to send the trade secret claims and tortious interference proceedings to arbitration. On August 12, 2004, ANSI amended its complaint to include two additional patents. On January 25, 2005, the Court granted, in part, the motion to move the misappropriation of trade secrets and tortious interference claims to arbitration. On March 11, 2005, Advanced Bionics answered the amended complaint, denying the allegations and filed a counterclaim against ANSI alleging that certain products sold by ANSI infringe two patents owned by Advanced Bionics. The counterclaim seeks monetary and injunctive relief. A patent claim interpretation hearing was held on April 15, 2005. On May 18, 2005, the Court granted ANSI's motion to sever the patents alleged in Advanced Bionics' counterclaim. On January 31, 2006, the judge ruled that ANSI's patent claims against Advanced Bionics will not be heard until the completion of the arbitration proceedings relating to trade secret claims. A trial on the Advanced Bionics patent claims has been scheduled for November 2006. Arbitration in the trade secret claims has not yet been scheduled. During the fourth quarter of 2005, ANSI was acquired by St. Jude Medical, Inc.

Litigation with Medinol Ltd.

On September 21, 2005, the Company and Medinol reached a settlement effectively resolving all outstanding stent litigation between the parties. Under the terms of the settlement, the Company paid Medinol $750 million, and the parties agreed to a mutual release of most existing claims against each other, including all disputes with respect to the Express and TAXUS Express stents, the termination of all agreements between each other, including the supply agreement, the cancellation of the Company's equity investment in Medinol, the establishment of an arbitration process to be the sole forum to hear any future disputes that may arise involving certain Medinol patents, in which Medinol has agreed to limit any relief it seeks to reasonable royalties, and a covenant by Medinol not to sue the Company under certain Medinol patents other than through the established arbitration process.

On September 10, 2002, the Company filed suit against Medinol alleging Medinol's NIRFlex™ stent and NIRFlex™ Royal stent products infringe two patents owned by the Company. The suit was filed in Dusseldorf, Germany seeking monetary and injunctive relief. On October 28, 2003, the German Court found that Medinol infringed one of the two patents owned by the Company. On December 8, 2003, the Company filed an appeal relative to the other patent. Subsequently, Medinol filed an appeal relative to the one patent found to be infringed. A hearing was held on both appeals on April 14, 2005. The Court had requested an expert to provide more evidence. A hearing has not yet been scheduled.

On September 25, 2002, the Company filed suit against Medinol alleging Medinol's NIRFlex™ and NIRFlex™ Royal products infringe a patent owned by the Company. The suit was filed in the District Court of The Hague, The Netherlands seeking cross-border, monetary and injunctive relief. On September 10, 2003, the Dutch Court ruled that the patent was invalid. The Company appealed the Court's decision in December 2003. A hearing on the appeal has not yet been scheduled.

On February 20, 2006, Medinol submitted a request for arbitration against the Company, Boston Scientific Ltd. and Boston Scientific Scimed, Inc. pursuant to the settlement agreement between

Medinol and the Company dated September 21, 2005. The request for arbitration alleges that the Company's Liberté coronary stent system infringes two U.S. patents and one European patent owned by Medinol. Medinol is seeking to have the patents declared valid and enforceable and a reasonable royalty. The September 2005 settlement agreement provides, among other things, that Medinol may only seek reasonable royalties and is specifically precluded from seeking injunctive relief. As a result, the Company does not expect the outcome of this proceeding to have a material impact on the continued sale of the Liberté™ stent system internationally or in the United States, the continued sale of the TAXUS® Liberté™ stent system internationally or the launch of the TAXUS® Liberté™ stent system in the United States. The Company plans to defend against Medinol's claims vigorously.

Other Patent Litigation

On July 28, 2000, Dr. Tassilo Bonzel filed a complaint naming certain of the Company's Schneider Worldwide subsidiaries and Pfizer Inc. and certain of its affiliates as defendants, alleging that Pfizer failed to pay Dr. Bonzel amounts owed under a license agreement involving Dr. Bonzel's patented Monorail® balloon catheter technology. The suit was filed in the U.S. District Court for the District of Minnesota seeking monetary relief. On September 26, 2001, Dr. Bonzel and the Company reached a contingent settlement involving all but one claim asserted in the complaint. The contingency has been satisfied and the settlement is now final. On December 17, 2001, the remaining claim was dismissed without prejudice with leave to refile the suit in Germany. Dr. Bonzel filed an appeal of the dismissal of the remaining claim. On July 29, 2003, the Appellate Court affirmed the lower court's dismissal, and on October 24, 2003, the Minnesota Supreme Court denied Dr. Bonzel's petition for further review. On March 26, 2004, Dr. Bonzel filed a similar complaint against the Company, certain of its subsidiaries and Pfizer in the Federal District Court for the District of Minnesota. The Company and its subsidiaries answered, denying the allegations of the complaint. The Company filed a motion to dismiss the case and a hearing on the motion was held on August 27, 2004. On November 2, 2004, the Court granted the Company's motion and the case was dismissed with prejudice. On February 7, 2005, Dr. Bonzel appealed the Court's decision. A hearing on the appeal was held on October 25, 2005.

On September 12, 2002, EV3 Inc. filed suit against The Regents of the University of California and a subsidiary of the Company in the District Court of The Hague, The Netherlands, seeking a declaration that EV3's EDC II and VDS embolic coil products do not infringe three patents licensed to the Company from The Regents. On October 22, 2003, the Court ruled that the EV3 products infringe three patents licensed to the Company. On December 18, 2003, EV3 appealed the Court's ruling. A hearing has not yet been scheduled.

On March 29, 2005, the Company and Boston Scientific Scimed, Inc. filed suit against EV3 for patent infringement, alleging that EV3's SpideRX™ embolic protection device infringes four U.S. patents owned by the Company. The complaint was filed in the U.S. District Court for the District of Minnesota seeking monetary and injunctive relief. On May 9, 2005, EV3 answered the complaint, denying the allegations, and filed a counterclaim alleging that certain of the Company's embolic protection devices infringe a patent owned by EV3. The counterclaim also seeks a declaratory judgment of invalidity, unenforceability and non-infringement. Trial is expected to begin on February 1, 2007.

On December 16, 2003, The Regents filed suit against Micro Therapeutics, Inc. and Dendron GmbH alleging that Micro Therapeutics' Sapphire™ detachable coil delivery systems infringe twelve patents licensed to the Company and owned by The Regents. The complaint was filed in the U.S. District Court for the Northern District of California seeking monetary and injunctive relief. On January 8, 2004, Micro Therapeutics and Dendron filed a third-party complaint to include the Company and Target as third-party defendants seeking a declaratory judgment of invalidity and noninfringement with respect to the patents and antitrust violations. On February 17, 2004, the Company, as a third-party defendant, filed a motion to dismiss the Company from the case. On July 9, 2004, the Court granted the Company's motion in part and dismissed the Company and Target from the claims relating only to patent infringement, while denying dismissal of an antitrust claim. Motions for summary judgment are pending.

On September 27, 2004, the Company and a subsidiary filed suit for patent infringement against Micrus Corporation alleging that certain detachable embolic coil devices infringe two U.S. patents exclusively licensed to the subsidiary. The complaint was filed in the U.S. District Court for the Northern District of California seeking monetary and injunctive relief. On November 16, 2004, Micrus answered and filed counterclaims seeking a declaration of invalidity, unenforceability and noninfringement and included allegations of infringement against the Company relating to three U.S. patents owned by Micrus, and antitrust violations. On January 10, 2005, the Company filed a motion to dismiss certain of Micrus' counterclaims, and on February 23, 2005, the Court granted a request to stay the proceedings

pending a reexamination of the Company's patents by the U.S. Patent and Trademark Office.

On November 4, 2004, Applied Hydrogel Technology (AHT) and Dr. Lih-Bin Shih filed a complaint against Medluminal Systems, Inc., InterWest Partners, the Company and three individuals alleging that certain of Medluminal's products infringe a patent owned by AHT. The complaint also includes claims of misappropriation of trade secrets and conversion against the Company and certain of the other defendants. The suit was filed in the U.S. District Court for the Southern District of California seeking monetary and injunctive relief. On February 15, 2005, the case was stayed pending arbitration proceedings. In January 2006, the parties agreed to dismiss the case, and on February 23, 2006, the case was dismissed with prejudice.

On February 1, 2005, the Company and Angiotech Pharmaceuticals, Inc. filed suit against Conor Medical System, Inc. in The Hague, The Netherlands seeking a declaration that Conor's drug-eluting stent products infringe patents owned by Angiotech and licensed to the Company. A hearing date has not yet been scheduled.

On November 8, 2005, the Company and Scimed filed suit against Conor alleging that certain of Conor's stent and drug-coated stent products infringe a patent owned by the Company. The complaint was filed in the U.S. District Court for the District of Delaware seeking monetary and injunctive relief. On December 30, 2005, Conor answered the complaint, denying the allegations.

On November 26, 2005, the Company and Angiotech filed suit against Occam International, BV in The Hague, Netherlands seeking a preliminary injunction against Occam's drug-eluting stent products based on infringement of patents owned by Angiotech and licensed to the Company. A hearing was held January 13, 2006, and on January 27, 2006, the Court denied the Company's request for a preliminary injunction. The Company plans to pursue normal infringement proceedings against Occam in The Netherlands.

On December 16, 2005, Bruce N. Saffran, M.D., Ph.D. filed suit against the Company alleging the Company's TAXUS® Express™ coronary stent system infringes a patent owned by Dr. Saffran. The suit was filed in the U.S. District Court for the Eastern District of Texas and seeks monetary and injunctive relief. On February 8, 2006, the Company filed an answer, denying the allegations of the complaint.

On April 4, 2005, the Company and Angiotech filed suit against Sahajanand Medical Technologies Pvt. Ltd. in The Hague, Netherlands seeking a declaration that Sahajanand's drug-eluting stent products infringe patents owned by Angiotech and licensed to the Company. A hearing is scheduled for March 10, 2006.

On May 19, 2005, G. David Jang, M.D. filed suit against the Company alleging breach of contract relating to certain patent rights assigned to the Company covering stent technology. The suit was filed in the U.S. District Court, Central District of California seeking monetary damages and recision of the contract. On June 24, 2005, the Company answered, denying the allegations, and filed a counterclaim.

On September 7, 2005, Dr. Shaun L. W. Samuels filed suit against the Company alleging misappropriation of trade secrets, unfair competition and that one of the Company's development-stage products infringes a patent owned by Dr. Samuels. The suit was filed in the U.S. District Court, Eastern District of Texas seeking monetary damages and injunctive relief. On November 2, 2005, the Company answered and filed counterclaims for declaratory judgment of non-infringement and invalidity. Trial is expected to begin in December 2006.

Department of Justice Investigation

In October 1998, the Company recalled its NIR ON® Ranger with Sox coronary stent delivery system following reports of balloon leaks. Since November 1998, the U.S. Department of Justice had been conducting an investigation primarily regarding: the shipment, sale and subsequent recall of the NIR ON® Ranger with Sox stent delivery system; aspects of its relationship with Medinol, the vendor of the stent; and related events. On June 24, 2005, the Company entered into a civil settlement with the U.S. Department of Justice. As part of the agreement, the Company agreed to pay $74 million. Also pursuant to the agreement, the Department of Justice filed a complaint in the U.S. District Court for the District of Massachusetts together with a Notice of Dismissal with prejudice. No charges were brought against the Company or any employee. The settlement involves no admission of any wrongdoing by the Company or any of its employees. The Company believes it acted legally, responsibly and appropriately at all times.

Other Proceedings

On January 10, 2002 and January 15, 2002, Alan Schuster and Antoinette Loeffler, respectively, putatively initiated shareholder derivative lawsuits for and on behalf of the Company in the U.S. District Court for the Southern District of New York against the Company's then current directors and the Company as nominal defendant. Both complaints allege, among other things, that with regard to the Company's relationship with Medinol, the defend-

ants breached their fiduciary duties to the Company and its shareholders in the management and affairs of the Company, and in the use and preservation of the Company's assets. The suits seek a declaration of the directors' alleged breach, damages sustained by the Company as a result of the alleged breach and monetary and injunctive relief. On October 18, 2002, the plaintiffs filed a consolidated amended complaint naming two senior officials as defendants and the Company as nominal defendant. The action was stayed in February 2003 pending resolution of a separate lawsuit brought by Medinol against the Company. After the resolution of the Medinol lawsuit, plaintiffs filed a motion in February 2006 seeking permission to file an amended complaint to supplement the allegations in the prior consolidated amended complaint based mainly on events that occurred subsequent to the parties' agreement to stay the action. The plaintiffs' motion remains pending.

On September 8, 2005, the Laborers Local 100 and 397 Pension Fund initiated a putative shareholder derivative lawsuit for and on behalf of the Company in the Commonwealth of Massachusetts Superior Court Department for Middlesex County against the Company's directors, certain of its current and former officers and the Company as nominal defendant. The complaint alleges, among other things, that with regard to certain matters of regulatory compliance, the defendants breached their fiduciary duties to the Company and its shareholders in the management and affairs of the Company and in the use and preservation of the Company's assets. The complaint also alleges that as a result of the alleged misconduct and the purported failure to publicly disclose material information, certain directors and officers sold Company stock at inflated prices in violation of their fiduciary duties and were unjustly enriched. The suits seek a declaration of the directors' and officers' alleged breaches, unspecified damages sustained by the Company as a result of the alleged breaches and other unspecified equitable and injunctive relief. On September 15, 2005, Benjamin Roussey also initiated a putative shareholder derivative lawsuit in the same Court alleging similar misconduct and seeking similar relief. The Company believes the suits will be consolidated. In November 2005, the Company filed a motion to transfer the cases to the Superior Court Business Litigation Session in Suffolk County. The Company's motions to transfer these cases to the Business Litigation Session were denied at a hearing held on these motions on January 11, 2006. The Company intends to appeal this decision to a single justice of Appeals Court for the Commonwealth of Massachusetts. The Board of Directors of the Company also received a letter dated January 17, 2006, on behalf of Benjamin Roussey regarding the Company's proposal to acquire Guidant Corporation. Mr. Roussey cited the pending litigation against Guidant and the potential liability it could face in the event of adverse outcomes to these matters and asked that the Board to Directors direct the Company to retract its offer to acquire Guidant before Guidant formally accepted it. The Board of Directors considered Mr. Roussey's request and ultimately approved the execution of the merger agreement with Guidant.

On September 23, 2005, Srinivasan Shankar, on behalf of himself and all others similarly situated, filed a purported securities class action suit in the U.S. District Court for the District of Massachusetts on behalf of those who purchased or otherwise acquired the Company's securities during the period March 31, 2003 through August 23, 2005, alleging that the Company and certain of its officers violated certain sections of the Securities Exchange Act of 1934. The complaint principally alleges that the Company did not adequately disclose its ability to satisfy FDA regulations governing medical device product quality, which resulted in the artificial inflation of the Company's stock price and enabled certain of the Company's officers to profit from the sale of Company stock at such inflated prices. The complaint seeks unspecified damages and equitable and injunctive relief. On September 28, 2005, October 27, 2005, November 2, 2005 and November 3, 2005, Jack Yopp, Robert L. Garber, Betty C. Meyer and John Ryan, respectively, on behalf of themselves and all others similarly situated, filed purported securities class action suits in the same Court on behalf of the same purported class, alleging similar misconduct and seeking similar relief. On November 21, 2005, six plaintiffs or plaintiff groups filed motions for consolidation, appointment of lead plaintiff and selection of lead counsel. The Court held a hearing on these motions on February 9, 2006. On February 15, 2006, the Court ordered that the five class actions be consolidated and appointed the Mississippi Public Employee Retirement System Group as lead plaintiff.

On January 19, 2006, George Larson, on behalf of himself and all others similarly situated, filed a purported class action complaint in the U.S. District Court for the District of Massachusetts on behalf of participants and beneficiaries of the Company's 401(k) Plan and GESOP, together the "Plans", during the period March 31, 2003 through January 19, 2006, alleging that the Company and certain of its officers and employees violated certain provisions under the Employee Retirement Income Security Act of 1974, as amended (ERISA) and Department of Labor Regulations. The complaint principally alleges that the defendants breached their fiduciary duties to the Plans' participants, failed to disclose adverse information about the Company to the Plans' participants and imprudently made contributions to the Company's 401(k) plan and GESOP in the form of Company stock. The

complaint seeks unspecified damages, and equitable and injunctive relief. On January 26, 2006, February 8, 2006, February 14, 2006 and February 23, 2006, Robert Hochstadt, Jeff Klunke, Kirk Harvey and Michael Lowe, respectively, on behalf of themselves and others similarly situated, filed purported class action complaints in the same court on behalf of the participants and beneficiaries in the Company's Plans. These complaints allege similar misconduct under ERISA and seek similar relief.

On January 26, 2006, Donald Wright filed a purported class action complaint in the U.S. District Court for the District of Minnesota against the Company and Guidant on behalf of himself and all other senior citizens and handicapped persons similarly situated seeking a permanent injunction to prohibit the Company from completing its acquisition of Guidant, alleging violations of the Minnesota Fraudulent Transfers Act and Consumer Fraud Act. The complaint seeks restitution on behalf of those persons who suffered injury related to Guidant's cardiac pacemakers and/or defibrillators. The complaint also seeks monetary damages and injunctive relief. Mr. Wright filed an amended complaint on February 21, 2006, dropping his claim for monetary damages. On February 14, 2006, Donald Wright filed a motion for preliminary and permanent injunction directing the Company to interplead $6.3 billion of the $27 billion purchase price to be paid to stockholders of Guidant. The motion alleges violations of the Minnesota Fraudulent Transfers Act and Consumer Fraud Act. The Company has not yet answered the complaint or responded to the February motion, but intends to vigorously deny the allegations.

On March 3, 2005, the African Assistance Program filed a charge of discrimination with the Minnesota Department of Human Rights and the Minnesota office of the U.S. Equal Employment Opportunity Commission, purportedly on behalf of certain of the Company's black employees of African national origin, alleging that the Company subjects black employees to a hostile work environment and discriminatory employment practices in violation of Title VII of the Civil Rights Act of 1964, as amended. The Company has denied liability in the action.

FDA Warning Letter

On January 26, 2006, the Company received a corporate warning letter from the FDA notifying the Company of serious regulatory problems at three facilities and advising the Company that its corporate wide corrective action plan relating to three warning letters issued to the Company in 2005 was inadequate. As also stated in this FDA warning letter, the FDA will not grant the Company's requests for exportation certificates to foreign governments or approve pre-market approval applications for its class III devices to which the quality control or current good manufacturing practices deficiencies described in the letter are reasonably related until the deficiencies described in the letter have been corrected. While the Company believes it can remediate these issues in an expeditious manner, there can be no assurances regarding the length of time it will take to resolve these issues, and any such resolution may require the dedication of significant incremental internal and external resources. In addition, if the Company's remedial actions are not satisfactory to the FDA, the FDA may take further regulatory actions against the Company, including but not limited to seizing its product inventory, obtaining a court injunction against further marketing of its products or assessing civil monetary penalties.

Note K – Stockholders' Equity

Preferred Stock

The Company is authorized to issue 50 million shares of preferred stock in one or more series and to fix the powers, designations, preferences and relative participating, option or other rights thereof, including dividend rights, conversion rights, voting rights, redemption terms, liquidation preferences and the number of shares constituting any series, without any further vote or action by the Company's stockholders. At December 31, 2005 and December 31, 2004, the Company had no shares of preferred stock issued or outstanding.

Common Stock

The Company is authorized to issue 1,200 million shares of common stock, $.01 par value per share. Holders of common stock are entitled to one vote per share. Holders of common stock are entitled to receive dividends if and when declared by the Board of Directors and to share ratably in the assets of the Company legally available for distribution to its stockholders in the event of liquidation. Holders of common stock have no preemptive, subscription, redemption, or conversion rights. The holders of common stock do not have cumulative voting rights. The holders of a majority of the shares of common stock can elect all of the directors and can control the management and affairs of the Company.

The Company paid a two-for-one stock split that was effected in the form of a 100 percent stock dividend on November 5, 2003. All historical share and per share amounts have been restated to reflect the stock split except for share amounts presented in the consolidated statements of stockholders' equity, which reflect the actual share amounts outstanding for each period presented.

The Company repurchased approximately 25 million shares of its common stock at an aggregate cost of $734 million in 2005, 10 million shares of its common stock at an aggregate cost of $360 million in 2004, and 22 million shares of its common stock at an aggregate cost of $570 million in 2003. Since 1992, the Company has repurchased approximately 132 million shares of its common stock and has approximately 24 million shares of common stock held in treasury at year end. Approximately 37 million shares remain under previous share repurchase authorizations. Repurchased shares are available for reissuance under the Company's equity incentive plans and for general corporate purposes, including strategic alliances and acquisitions.

Note L – Stock Ownership Plans

Employee and Director Stock Incentive Plans

The Company's 1995, 2000 and 2003 Long-Term Incentive Plans (Plans) provide for the issuance of up to 150 million shares of common stock. Together, the Plans cover officers, directors and employees of and consultants to the Company and provide for the grant of various incentives, including qualified and non-qualified options, deferred stock units, stock grants, share appreciation rights and performance awards. Nonqualified options granted to purchase shares of common stock are either immediately exercisable or exercisable in installments as determined by the Executive Compensation and Human Resources Committee of the Board of Directors (Committee), consisting of independent, non-employee directors, and expire within ten years from date of grant. Nonqualified options issued to employees generally have a vesting term over a period of three to five years. In the case of qualified options, if the recipient owns more than 10 percent of the voting power of all classes of stock, the option granted will be at an exercise price of 110 percent of the fair market value of the Company's common stock on the date of grant and will expire over a period not to exceed five years. The Committee may issue shares of common stock and authorize cash awards under the Plans in recognition of the achievement of long-term performance objectives established by the Committee. The 1995 Long-Term Incentive Plan expired in March 2005, after which time grants were issued under the 2000 and 2003 Long-Term Incentive Plans. Following the expiration of the 1995 Long-Term Incentive Plan, 90 million shares of common stock remain available for issuance under the Company's Plans.

During the fourth quarter of 2004, the Company modified certain of its stock option plans, principally for options granted prior to May 2001, to change the definition of retirement to conform to the definition generally used in the Company's stock option plans subsequent to May 2001. As a result of these modifications, the Company recorded a $90 million charge ($60 million after-tax) in 2004. The key assumptions in estimating the charge were the anticipated retirement age and the expected exercise patterns for the individuals whose options were modified.

Information related to stock options at December 31 under stock incentive plans is as follows:

	2005		2004		2003	
(option amounts in thousands)	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding at January 1	49,028	$17.84	66,103	$15.16	84,218	$12.23
Granted	7,983	30.12	2,101	39.72	6,857	33.33
Exercised	(5,105)	11.93	(18,296)	10.64	(24,023)	10.10
Canceled	(1,621)	28.24	(880)	18.41	(949)	13.86
Outstanding at December 31	**50,285**	**20.06**	**49,028**	**17.84**	**66,103**	**15.16**
Exercisable at December 31	**36,072**	**$15.96**	**34,776**	**$14.32**	**42,126**	**$12.01**

Information related to stock options outstanding and exercisable at December 31, 2005 is as follows:

	Stock Options Outstanding			Stock Options Exercisable	
Range of Exercise Prices	Options (in thousands)	Weighted Average Remaining Contractual Life (in years)	Weighted Average Exercise Price	Options (in thousands)	Weighted Average Exercise Price
$ 0.00 – 8.00	3,612	4.96	$ 6.21	3,612	$ 6.21
8.01 – 16.00	17,179	4.10	11.92	17,081	11.91
16.01 – 24.00	14,339	5.15	19.78	12,068	19.49
24.01 – 32.00	4,725	9.38	27.21	178	31.04
32.01 – 40.00	9,284	8.37	34.59	3,098	34.77
40.01 – 48.00	1,146	8.43	41.95	35	41.67
	50,285	**5.85**	**$20.06**	**36,072**	**$15.96**

Shares reserved for future issuance under all of the Company's stock incentive plans totaled approximately 90 million at December 31, 2005.

A table illustrating the effect on net income and net income per share as if the fair value method prescribed by Statement No. 123 had been applied is presented in *Note A—Significant Accounting Policies*. The Company recognizes any compensation cost on fixed awards with pro rata vesting on a straight-line basis over the award's vesting period. The fair value of the stock options used to calculate the pro forma net income and net income per share was

estimated using the Black-Scholes option-pricing model with the following weighted average assumptions:

	2005	2004	2003
Dividend yield	0%	0%	0%
Expected volatility	36.64%	46.85%	49.28%
Risk-free interest rate	3.76%	3.50%	3.13%
Forfeitures	687,000	615,000	632,000
Expected life	5	5	5

The weighted average grant-date fair value per share of options granted, calculated using the Black-Scholes option-pricing model, was $12.18 in 2005, $14.36 in 2004 and $14.96 in 2003.

In 2005, the Company granted approximately 3.9 million deferred stock units to its employees under its stock incentive plans at a weighted average fair value of $30.77. The market value of the shares underlying the deferred stock units was approximately $119 million on the date of issuance. The deferred stock units vest over a period of five to six years. The amount was recorded as deferred compensation and shown as a separate component of stockholders' equity. The deferred compensation is being amortized to expense over the vesting period, and the related expense amounted to $17 million for 2005. During 2005, the Company reversed approximately $5 million of deferred compensation associated with forfeitures of these deferred stock units.

Global Employee Stock Ownership Plan

The Company's GESOP provides for the granting of options to purchase up to 15 million shares of the Company's common stock to all eligible employees. Under the GESOP, each eligible employee is granted, at the beginning of each period designated by the Committee as an offering period, an option to purchase shares of the Company's common stock equal to not more than 10 percent of the employee's eligible compensation or the statutory limit under the U.S. Internal Revenue Code. Such options may be exercised generally only to the extent of accumulated payroll deductions at the end of the offering period, at a purchase price equal to 85 percent of the fair market value of the Company's common stock at the beginning or end of each offering period, whichever is less.

Information related to the shares issued under the GESOP and the range of purchase prices is as follows:

	2005	2004	2003
Shares issued	1,445,000	1,004,000	1,228,000
Range of purchase prices	$20.82 - $22.95	$30.22 - $30.81	$12.21 - $18.27

At December 31, 2005, there were approximately two million shares available for future issuance under the GESOP plan. On February 28, 2006, the Board of Directors adopted, and recommended that the stockholders of the Company approve and adopt at the Company's 2006 Annual Meeting of Stockholders, the Company's 2006 GESOP, a new employee stock purchase plan that provides for the granting of options to purchase up to 20 million shares of the Company's common stock to all eligible employees. The terms and conditions of the 2006 GESOP are substantially similar to the existing GESOP, which expires by its terms in 2007.

Note M – Earnings per Share

The computation of basic and diluted earnings per share is as follows:

(in millions, except per share data)	2005	2004	2003
Basic			
Net income	$ 628	$1,062	$ 472
Weighted average shares outstanding	825.8	838.2	821.0
Net income per common share	**$ 0.76**	**$ 1.27**	**$ 0.57**
Assuming Dilution			
Net income	$ 628	$1,062	$ 472
Weighted average shares outstanding	825.8	838.2	821.0
Net effect of common stock equivalents	11.8	19.5	24.4
Total	837.6	857.7	845.4
Net income per common share	**$ 0.75**	**$ 1.24**	**$ 0.56**

Potential common stock equivalents of 12 million in 2005, one million in 2004 and one million in 2003 were excluded from the computation of earnings per share, assuming dilution, because exercise prices were greater than the average market price of the common shares.

Note N – Segment Reporting

The Company has four reportable operating segments based on geographic regions: the United States, Europe, Japan and Inter-Continental. Each of the Company's reportable segments generates revenues from the sale of less-invasive medical devices. The reportable segments represent an aggregate of all operating divisions within each segment.

Sales and operating results of reportable segments are based on internally derived standard foreign exchange rates, which may differ from year to year and do not include intersegment profits. The segment information for 2004 and 2003 sales and operating results have been restated based on the Company's standard foreign exchange rates used for 2005. Because of the interdependence of the reportable segments, the operating profit as presented may not be representative of the geographic dis-

tribution that would occur if the segments were not interdependent. Enterprise-wide information is based on actual foreign exchange rates used in the Company's consolidated financial statements.

(in millions)	United States	Europe	Japan	Inter-Continental	Total
2005					
Net sales	$3,852	$1,145	$579	$643	**$6,219**
Depreciation	18	4	3	4	**29**
Operating income allocated to reportable segments	1,803	598	308	295	**3,004**
2004					
Net sales	$3,502	$ 980	$602	$501	**$5,585**
Depreciation	9	5	3	2	**19**
Operating income allocated to reportable segments	1,753	507	343	227	**2,830**
2003					
Net sales	$1,924	$ 729	$568	$348	**$3,569**
Depreciation	8	3	3	2	**16**
Operating income allocated to reportable segments	682	356	323	148	**1,509**

A reconciliation of the totals reported for the reportable segments to the applicable line items in the consolidated financial statements is as follows:

(in millions)	2005	2004	2003
Net Sales			
Total net sales allocated to reportable segments	$6,219	$5,585	$3,569
Foreign exchange	64	39	(93)
	$6,283	**$5,624**	**$3,476**
Depreciation			
Total depreciation allocated to reportable segments	$ 29	$ 19	$ 16
Manufacturing operations	89	113	69
Corporate expenses and foreign exchange	44	31	22
	$ 162	**$ 163**	**$ 107**
Income before Income Taxes			
Total operating income allocated to reportable segments	$3,004	$2,830	$1,509
Manufacturing operations	(448)	(394)	(305)
Corporate expenses and foreign exchange	(476)	(522)	(455)
Litigation-related charges	(780)	(75)	(15)
Purchased research and development	(276)	(65)	(37)
Costs of certain retirement benefits	(17)	(110)	
Stock-compensation charge for certain modifications		(90)	
Costs of certain business optimization initiatives	(39)		
	968	1,574	697
Other income (expense)	(77)	(80)	(54)
	$ 891	**$1,494**	**$ 643**

Enterprise-Wide Information

(in millions)	2005	2004	2003
Net Sales			
Cardiovascular	$4,907	$4,490	$2,504
Endosurgery	1,228	1,088	972
Neuromodulation	148	46	N/A
	$6,283	**$5,624**	**$3,476**
Long-Lived Assets			
United States	$ 795	$ 660	$ 536
Ireland	140	149	169
Other foreign countries	76	61	39
	$1,011	**$ 870**	**$ 744**

Note O – Subsequent Events

Guidant Transaction

On January 25, 2006, Boston Scientific entered into a definitive agreement to acquire Guidant Corporation for an aggregate purchase price of $27 billion (net of proceeds from option exercises), which represents a combination of cash and stock worth $80 per share of Guidant common stock. Guidant is a world leader in the treatment of cardiac and vascular disease. At the effective time of the acquisition, each share of Guidant common stock (other than shares owned by Guidant, Galaxy Merger Sub and Boston Scientific) will be converted into the right to receive (i) $42.00 in cash and (ii) a number of shares of Boston Scientific common stock equal to the actual exchange ratio. The actual exchange ratio will be determined by dividing $38.00 by the average closing price of Boston Scientific common stock during the 20 consecutive trading day period ending three trading days prior to the closing date, so long as the average closing price during that period is between $22.62 and $28.86. If the average closing price of Boston Scientific common stock during that period is less than $22.62, Guidant shareholders will receive 1.6799 Boston Scientific shares for each share of Guidant common stock, and if the average closing price of Boston Scientific common stock during that period is greater than $28.86, Guidant shareholders will receive 1.3167 Boston Scientific shares for each share of Guidant common stock. In addition, if the acquisition is not closed by March 31, 2006, Guidant shareholders will receive an additional $0.0132 in cash per share of Guidant common stock for each day beginning on April 1, 2006 through the closing date of the acquisition.

Outstanding Guidant stock options at the closing date of the merger will be converted into options to purchase Boston Scientific common stock, with appropriate adjustments made to the number of shares and the exercise price under those options based on the value of the merger consideration.

In addition, the combined company will incur integration and restructuring costs following the completion of the acquisition as Boston Scientific integrates certain operations of Guidant. Although Boston Scientific and Guidant expect that the realization of efficiencies related to the integration of the businesses may offset incremental transaction, merger-related and restructuring costs over time, no assurances can be made that this net benefit will be achieved in the near term, or at all.

In connection with the financing of the cash portion of the purchase price, various banks have committed to providing up to $14 billion in financing, which includes a $7 billion 364-day interim credit facility, a $5 billion five-year term loan facility and a $2 billion five-year revolving credit facility. The interim credit facility, term loan and revolving credit facility will bear interest at LIBOR plus an interest margin between 0.30 percent (high A rating) and 0.85 percent (low BBB rating). The interest margin will be based on the highest two out of three of the Company's long-term, senior unsecured, corporate credit ratings from Moody's Investor Service Inc., Standard & Poor's Rating Services and Fitch Ratings. Of the $14 billion available pursuant to the commitment letter, the Company expects to borrow approximately $7.1 billion to finance the cash portion of the Guidant acquisition purchase price, which includes the $5 billion five-year term loan facility and $2.1 billion in borrowings under the 364-day interim credit facility. The Company also expects to use the $900 million loan from Abbott, for a total of $8 billion in borrowings to finance the cash portion of the purchase price. In 2006, the Company anticipates filing a new public registration statement with the SEC under which it intends to issue senior notes in order to refinance any borrowings outstanding under the interim credit facility and to register shares that it will issue to Abbott. The new five-year revolving credit facility will replace the Company's existing $2 billion credit facilities. The Company also plans to use cash on hand and cash from the Abbott transaction to fund the cash portion of the Guidant purchase price.

Boston Scientific's offer to acquire Guidant was made after the execution of a merger agreement among Guidant, Johnson & Johnson and Shelby Merger Sub, Inc. On January 25, 2006, Guidant terminated the Johnson & Johnson merger agreement and, in connection with the termination, Guidant paid Johnson & Johnson a termination fee of $705 million. Boston Scientific then reimbursed Guidant for the full amount of the termination fee paid to Johnson & Johnson.

In conjunction with the proposed acquisition, Boston Scientific's authorized common stock will be increased from 1,200,000,000 shares to 2,000,000,000 shares. The transaction is subject to customary closing conditions, including clearances under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 and the European Union merger control regulation, as well as approval of Boston Scientific and Guidant shareholders. The transaction is not subject to any financing condition. Subject to these conditions, it is currently expected that the acquisition will occur during the week of April 3, 2006.

Abbott Transaction

In January 2006, Boston Scientific and Abbott entered into the Abbott transaction agreement pursuant to which, among other things, Abbott agreed to purchase the Guidant vascular and endovascular businesses for:

- an initial payment of $4.1 billion in cash at the Abbott transaction closing;
- a milestone payment of $250 million upon receipt of an approval from the U.S. FDA within ten years after the Abbott transaction closing to market and sell an everolimus-eluting stent in the U.S.; and
- a milestone payment of $250 million upon receipt of an approval from the Japanese Ministry of Health within ten years after the Abbott transaction closing to market and sell an everolimus-eluting stent in Japan.

The Abbott transaction closing is subject to, among other things, the satisfaction or waiver of all of the conditions to close the Guidant transaction and is expected to occur prior to the closing date of the acquisition.

In addition to receiving the initial payment of $4.1 billion at the Abbott transaction closing, Abbott has agreed to lend Boston Scientific $900 million on a subordinated basis. The loan will be payable on the fifth anniversary of the Abbott transaction closing and interest will accrue on the outstanding principal amount at a rate of 4.00 percent per annum.

At the Abbott transaction closing, Abbott will also purchase $1.4 billion in shares of Boston Scientific common stock based on a per share purchase price of the lower of (i) $25.00 and (ii) the average closing price of Boston Scientific common stock during the five consecutive trading day period ending three trading days prior to the Abbott transaction closing. In addition, 18 months after the Abbott transaction closing, Boston Scientific will issue to Abbott additional shares of Boston Scientific common stock having an aggregate value of up to $60 million (based on the average closing price of Boston Scientific common stock during the 20 consecutive trading day period ending five trading days prior to the date of issuance of those shares) to reimburse Abbott

for the cost of borrowing $1.4 billion to purchase the shares of Boston Scientific common stock.

Abbott has agreed not to sell any of these shares of Boston Scientific common stock for six months following the Abbott transaction closing unless the average price per share of Boston Scientific common stock over any consecutive 20 day trading period exceeds $30.00. In addition, during the 18-month period following the Abbott transaction closing, Abbott will not, in any one-month period, sell more than 8.33 percent of these shares of Boston Scientific common stock. Abbott must apply a portion of the net proceeds from its sale of these shares of Boston Scientific common stock in excess of specified amounts, if any, to reduce the principal amount of the loan from Abbott to Boston Scientific.

As a part of the Abbott transaction, Boston Scientific and Abbott will also enter into supply and license and technology transfer arrangements with respect to the everolimus-based drug-eluting stent system currently in development by Guidant. This supply and license agreement will serve as collateral for the $900 million loan.

Outstanding options held by Guidant employees transferred to Abbott will, at Boston Scientific's election, either be converted into a number of shares of Boston Scientific common stock with a fair market value as of the Abbott transaction closing date equal to the excess of the aggregate fair market value of the Guidant common stock subject to the option over the exercise price of the option, net of applicable withholding taxes or exchanged for a cash payment equal to the excess of the aggregate fair market value of the Guidant common stock subject to the option over the aggregate exercise price of the option, net of any applicable withholding taxes.

As a result of the proposed Guidant transaction and Abbott transaction, current Boston Scientific stockholders will own a smaller percentage of Boston Scientific following the acquisition. The Company expects its weighted average shares outstanding, assuming dilution, to increase from approximately 840 million for 2005 to approximately 1.4 billion following the acquisition.

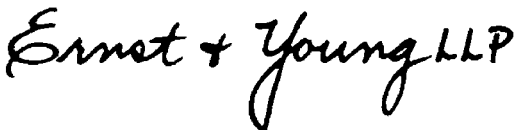
The Board of Directors and Stockholders of Boston Scientific Corporation

We have audited the accompanying consolidated balance sheets of Boston Scientific Corporation as of December 31, 2005 and December 31, 2004, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2005. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Boston Scientific Corporation at December 31, 2005 and December 31, 2004, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2005, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Boston Scientific Corporation's internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 24, 2006, expressed an unqualified opinion thereon.



Boston, Massachusetts
February 24, 2006

Year Ended December 31, (in millions, except per share data)	**2005**	**2004**	**2003**	**2002**	**2001**
Operating Data					
Net sales	$6,283	$5,624	$3,476	$2,919	$2,673
Gross profit	4,897	4,332	2,515	2,049	1,754
Selling, general and administrative expenses	1,814	1,742	1,171	1,002	926
Research and development expenses	680	569	452	343	275
Royalty expense	227	195	54	36	35
Amortization expense	152	112	89	72	136
Litigation-related charges (credits), net	780	75	15	(99)	
Purchased research and development	276	65	37	85	282
Total operating expenses	3,929	2,758	1,818	1,439	1,654
Operating income	968	1,574	697	610	100
Income before income taxes	891	1,494	643	549	44
Net income (loss)	628	1,062	472	373	(54)
Net income (loss) per common share—basic	$ 0.76	$ 1.27	$ 0.57	$ 0.46	$ (0.07)
Net income (loss) per common share—assuming dilution	$ 0.75	$ 1.24	$ 0.56	$ 0.45	$ (0.07)
Weighted average shares outstanding—assuming dilution	837.6	857.7	845.4	830.0	802.8

As of December 31, (in millions, except per share data)	**2005**	**2004**	**2003**	**2002**	**2001**
Balance Sheet Data					
Cash, cash equivalents and marketable securities	$ 848	$1,640	$ 752	$ 260	$ 185
Working capital	1,152	684	487	285	275
Total assets	8,196	8,170	5,699	4,450	3,974
Borrowings (long-term and short-term)	2,020	2,367	1,725	935	1,204
Stockholders' equity	4,282	4,025	2,862	2,467	2,015
Book value per common share	$ 5.22	$ 4.82	$ 3.46	$ 3.00	$2.49

The Company paid a two-for-one stock split that was effected in the form of a 100 percent stock dividend on November 5, 2003. All historical amounts above have been restated to reflect the stock split.

(See notes to the consolidated financial statements)

Three Months Ended (in millions, except per share data)	**March 31,**	**June 30,**	**September 30,**	**December 31,**
2005				
Net sales	$1,615	$1,617	$1,511	$1,540
Gross profit	1,271	1,260	1,168	1,198
Operating income (loss)	513	326	(336)	465
Net income (loss)	358	205	(269)	334
Net income (loss) per common share—basic	$ 0.43	$ 0.25	$ (0.33)	$ 0.41
Net income (loss) per common share—assuming dilution	$ 0.42	$ 0.24	$ (0.33)	$ 0.40
2004				
Net sales	$1,082	$1,460	$1,482	$1,600
Gross profit	790	1,097	1,173	1,272
Operating income	264	448	358	504
Net income	194	313	258	297
Net income per common share—basic	$ 0.23	$ 0.37	$ 0.31	$ 0.35
Net income per common share—assuming dilution	$ 0.23	$ 0.36	$ 0.30	$ 0.35

During 2005, the Company recorded after-tax charges of $73 million in the first quarter, $199 million in the second quarter, $616 million in the third quarter and $6 million in the fourth quarter. The net charges for the year consisted of: a litigation settlement with Medinol; purchased research and development; expenses related to certain retirement benefits; asset write-downs and employee-related costs that resulted from certain business optimization initiatives; and a benefit for a tax adjustment associated with a technical correction made to the American Jobs Creation Act.

During 2004, the Company recorded after-tax charges of $64 million in the second quarter, $146 million in the third quarter and $122 million in the fourth quarter. The net charges for the year consisted of: a provision for a civil settlement; an enhancement to the Company's 401(k) Plan; purchased research and development; a charge relating to taxes on the approximately $1 billion of cash that the Company repatriated in 2005 under the American Jobs Creation Act; and a non-cash charge resulting from certain modifications to the Company's stock option plans.

(See notes to the consolidated financial statements)

Our common stock is traded on the New York Stock Exchange under the symbol "BSX."

The following table shows the market range for our common stock for each of the last eight quarters based on reported sales prices on the New York Stock Exchange.

	High	Low
2005		
First Quarter	$35.19	$28.67
Second Quarter	30.80	27.00
Third Quarter	28.95	23.05
Fourth Quarter	27.33	22.95

	High	Low
2004		
First Quarter	$44.12	$35.86
Second Quarter	45.81	37.32
Third Quarter	42.70	32.12
Fourth Quarter	39.46	33.36

The Company has not paid a cash dividend during the past two years. The Company currently does not intend to pay dividends, and intends to retain all of our earnings to repay indebtedness and invest in the continued growth of its business. The Company may consider declaring and paying a dividend in the future; however, there can be no assurance that it will do so.

At February 22, 2006, there were 8,143 record holders of the Company's common stock.

(See notes to the consolidated financial statements)

EXECUTIVE OFFICERS AND DIRECTORS

John E. Abele
Director; Founder Chairman

Lawrence C. Best
Executive Vice President, Finance and Administration and Chief Financial Officer

Brian R. Burns
Senior Vice President, Quality

Ursula M. Burns[2, 4]
Director; President, Business Group Operations and Corporate Senior Vice President, Xerox Corporation

Fredericus A. Colen
Executive Vice President and Chief Technology Officer

Paul Donovan
Senior Vice President, Corporate Communications

Joel L. Fleishman[1, 3]
Director; Professor of Law and Public Policy, Duke University

Marye Anne Fox, Ph.D.[1, 4]
Director; Chancellor, University of California, San Diego

James Gilbert
Senior Vice President

Jeffrey H. Goodman
Senior Vice President, International

Ray J. Groves[2, 3]
Director; Retired President, Chairman and Senior Advisor, Marsh, Inc.

Paul A. LaViolette
Chief Operating Officer

Ernest Mario, Ph.D.[1, 4]
Director; Chairman and Chief Executive Officer, Reliant Pharmaceuticals, LLC

Stephen F. Moreci
Senior Vice President and Group President, Endosurgery

N.J. Nicholas, Jr.[4]
Director; Private Investor

Peter M. Nicholas
Director; Chairman of the Board

John E. Pepper[1, 4]
Director; Chief Executive Officer, National Underground Railroad Freedom Center and Retired Chairman and Chief Executive Officer, The Procter & Gamble Co.

Kenneth J. Pucel
Senior Vice President, Operations

Lucia L. Quinn
Executive Vice President, Human Resources

Uwe E. Reinhardt, Ph.D.[1, 3]
Director; Professor of Economics and Public Affairs, Princeton University

Warren B. Rudman[2, 3]
Director; Former U.S. Senator, Of Counsel, Paul, Weiss, Rifkind, Wharton & Garrison

Mary E. Russell, M.D.
Senior Vice President, Clinical and Regulatory and Chief Medical Officer

Paul W. Sandman
Executive Vice President, Secretary and General Counsel

James R. Tobin[4]
Director; President and Chief Executive Officer

CORPORATE HEADQUARTERS

Boston Scientific Corporation
One Boston Scientific Place
Natick, MA 01760-1537
508-650-8000
508-647-2200 (Investor Relations Facsimile)
www.bostonscientific.com

REGIONAL HEADQUARTERS

Boston Scientific Asia Pacific Pte. Ltd.
Singapore

Boston Scientific International S.A.
Paris, France

Boston Scientific Japan K.K.
Tokyo, Japan

TECHNOLOGY CENTERS

Cork, Ireland

Fremont, CA, U.S.A.

Galway, Ireland

Glens Falls, NY, U.S.A.

Heredia, Costa Rica

Kerkrade, The Netherlands

Letterkeny, Ireland

Los Gatos, CA, U.S.A.

Maple Grove, MN, U.S.A.

Marlborough, MA, U.S.A.

Miami, FL, U.S.A.

Miyazaki, Japan

Mountain View, CA, U.S.A.

Murietta, CA, U.S.A.

Natick, MA, U.S.A.

Plymouth, MN, U.S.A.

Quincy, MA, U.S.A.

Salt Lake City, UT, U.S.A.

San Diego, CA, U.S.A.

San Jose, CA, U.S.A.

Santa Rosa, CA, U.S.A.

Spencer, IN, U.S.A.

Sylmar, CA, U.S.A.

Tullamore, Ireland

Valencia, CA, U.S.A.

Watertown, MA, U.S.A.

Wayne, NJ, U.S.A.

STOCKHOLDER INFORMATION STOCK LISTING

Boston Scientific Corporation common stock is traded on the New York Stock Exchange under the symbol "BSX".

TRANSFER AGENT

Inquiries concerning the transfer or exchange of shares, lost stock certificates, duplicate mailings or changes of address should be directed to the Company's Transfer Agent at:

MELLON INVESTOR SERVICES LLC

480 Washington Boulevard
Jersey City, NJ 07310
1-800-898-6713
www.melloninvestor.com

INDEPENDENT AUDITORS

Ernst & Young LLP
Boston, Massachusetts

ANNUAL MEETING

The annual meeting of stockholders will take place on Tuesday, May 9, 2006, beginning at 10:00 a.m. at the Bank of America Northeast Conference and Training Center, 100 Federal Street, Boston, MA.

INVESTOR INFORMATION REQUESTS

Investors, stockholders and security analysts seeking information about the Company should refer to the Company's website at www.bostonscientific.com or call Investor Relations at 508-650-8555.

OTHER INFORMATION

Copies of the Company's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports are available free of charge through the Company's website at www.bostonscientific.com. Our Corporate Governance Guidelines, proxy statement and Code of Conduct, which applies to all of our directors, officers and employees, including our Board of Directors, Chief Executive Officer and Chief Financial Officer, are also available on our website.

The Company has included as exhibits to its annual report on Form 10-K for the fiscal year 2005 filed with the SEC certificates of its Chief Executive Officer and Chief Financial Officer certifying the quality of the Company's public disclosure, and our annual CEO certification for the previous year has been submitted to the New York Stock Exchange.

Copies of these reports are also available by directing requests to:

Investor Relations
Boston Scientific Corporation
One Boston Scientific Place
Natick, MA 01760-1537
508-650-8555
508-647-2200 *(Facsimile)*
Investor_Relations@bsci.com

1 *Member of the Audit Committee*
2 *Member of the Executive Compensation and Human Resources Committee*
3 *Member of the Nominating and Corporate Governance Committee*
4 *Member of the Finance and Strategic Investment Committee*

This annual report has been produced at an ISO 14001 certified printing plant. It is produced on paper that contains a minimum of 10% post consumer waste and up to 50% recycled content. The paper is elemental chlorine free.

Boston Scientific

Delivering what's next.™

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