APPLERA CORP
Form 10-Q
November 07, 2007


**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

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# FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
**For the quarterly period ended September 30, 2007**

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission file number: **001-04389**

## APPLERA CORPORATION

(Exact Name of Registrant as Specified in Its Charter)

| | |
|---|---|
| **Delaware** | **06-1534213** |
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification No.) |
| **301 Merritt 7, Norwalk, Connecticut** | **06851-1070** |
| (Address of Principal Executive Offices) | (Zip Code) |

**(203) 840-2000**

(Registrant s Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No ¨

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

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

As of the close of business on November 1, 2007, there were 168,184,055 shares of Applera Corporation-Applied Biosystems Group Common Stock and 79,370,805 shares of Applera Corporation-Celera Group Common Stock outstanding.

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**PART I FINANCIAL INFORMATION**

**Item 1. Financial Statements.**

**APPLERA CORPORATION**

**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

**(unaudited)**

**(Dollar amounts in thousands except per share amounts)**

| | Three Months Ended September 30, | |
|---|---|---|
| | **2007** | 2006 |
| Products | **$ 407,492** | $ 391,082 |
| Services | **64,373** | 58,140 |
| Other | **44,808** | 36,187 |
| **Total Net Revenues** | **516,673** | 485,409 |
| Products | **192,579** | 196,659 |
| Services | **28,747** | 24,598 |
| Other | **2,901** | 2,827 |
| **Total Cost of Sales** | **224,227** | 224,084 |
| **Gross Margin** | **292,446** | 261,325 |
| Selling, general and administrative | **156,494** | 142,385 |
| Research and development | **60,809** | 57,902 |
| Amortization of purchased intangible assets | **2,612** | 2,737 |
| Employee-related charges, asset impairments and other | | 3,500 |
| Asset dispositions and legal settlements | **(7,556)** | 9,087 |
| Acquired research and development | | 114,251 |
| **Operating Income (Loss)** | **80,087** | (68,537) |
| Gain on investments, net | | 209 |
| Interest expense | **(1,356)** | (497) |
| Interest income | **12,169** | 9,710 |
| Other income (expense), net | **787** | 1,417 |
| **Income (Loss) before Income Taxes** | **91,687** | (57,698) |
| Provision for income taxes | **29,997** | 8,314 |
| **Net Income (Loss)** | **$ 61,690** | $ (66,012) |
| **Applied Biosystems Group (see Note 4)** | | |
| **Net Income (Loss) per Share** | | |
| Basic | **$ 0.33** | $ (0.32) |
| Diluted | **$ 0.32** | $ (0.32) |
| **Dividends Declared per Share** | **$ 0.0425** | $ 0.0425 |

| | | |
|---|---|---|
| **Celera Group (see Note 4)** | | |
| **Net Income (Loss) per Share** | | |
| Basic and diluted | **$ 0.01** | $ (0.09) |

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

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**APPLERA CORPORATION**

**CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**

**(unaudited)**

**(Dollar amounts in thousands)**

| | At September 30, 2007 | At June 30, 2007 |
|---|---|---|
| **Assets** | | |
| Current assets | | |
| Cash and cash equivalents | **$ 464,437** | $ 323,203 |
| Short-term investments | **360,874** | 732,757 |
| Accounts receivable, net | **430,129** | 452,873 |
| Inventories, net | **157,878** | 140,349 |
| Prepaid expenses and other current assets | **173,852** | 189,405 |
| Total current assets | **1,587,170** | 1,838,587 |
| Property, plant and equipment, net | **386,381** | 390,810 |
| Goodwill and intangible assets, net | **303,010** | 304,812 |
| Other long-term assets | **636,062** | 618,331 |
| **Total Assets** | **$ 2,912,623** | $ 3,152,540 |
| **Liabilities and Stockholders Equity** | | |
| Current liabilities | | |
| Loans payable | **$ 275,000** | $ - |
| Accounts payable | **153,792** | 162,665 |
| Accrued salaries and wages | **60,151** | 108,552 |
| Current deferred tax liability | **16,149** | 15,633 |
| Accrued taxes on income | **17,057** | 66,701 |
| Other accrued expenses | **281,831** | 269,623 |
| Total current liabilities | **803,980** | 623,174 |
| Other long-term liabilities | **269,343** | 213,312 |
| **Total Liabilities** | **1,073,323** | 836,486 |
| **Stockholders Equity** | | |
| Capital stock | | |
| Applera Corporation Applied Biosystems Group | **2,133** | 2,133 |
| Applera Corporation Celera Group | **793** | 790 |
| Capital in excess of par value | **2,253,871** | 2,248,372 |
| Retained earnings | **946,133** | 854,721 |
| Accumulated other comprehensive income | **15,080** | 11,363 |
| Treasury stock, at cost | **(1,378,710)** | (801,325) |
| **Total Stockholders Equity** | **1,839,300** | 2,316,054 |
| **Total Liabilities and Stockholders Equity** | **$ 2,912,623** | $ 3,152,540 |

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

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**APPLERA CORPORATION**

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

**(unaudited)**

**(Dollar amounts in thousands)**

| | Three months ended September 30, 2007 | 2006 |
|---|---|---|
| **Operating Activities of Continuing Operations** | | |
| Net income (loss) | **$ 61,690** | $ (66,012) |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | | |
| Depreciation and amortization | **20,025** | 21,079 |
| Employee-related charges and other | | 3,500 |
| Share-based compensation and pension | **7,001** | 4,503 |
| Deferred income taxes | **20,277** | (3,670) |
| Sale of assets and legal settlements, net | | (209) |
| Acquired research and development | | 114,251 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | **37,502** | 41,510 |
| Inventories | **(17,153)** | (5,139) |
| Prepaid expenses and other assets | **11,043** | (16,281) |
| Accounts payable and other liabilities | **(57,653)** | (84,867) |
| **Net Cash Provided by Operating Activities of Continuing Operations** | **82,732** | 8,665 |
| **Net Cash Provided by Discontinued Operations** | **12,900** | |
| **Investing Activities of Continuing Operations** | | |
| Additions to property, plant and equipment, net | **(9,758)** | (14,911) |
| Proceeds from maturities of available-for-sale investments | **30,409** | 40,870 |
| Proceeds from sales of available-for-sale investments | **396,692** | 115,800 |
| Purchases of available-for-sale investments | **(55,259)** | (212,585) |
| Acquisitions and investments | **(179)** | (121,403) |
| Proceeds from the sale of assets, net | | 322 |
| **Net Cash Provided (Used) by Investing Activities of Continuing Operations** | **361,905** | (191,907) |
| **Financing Activities** | | |
| Proceeds from loans payable | **275,000** | |
| Dividends | **(7,745)** | (7,647) |
| Purchases of common stock for treasury | **(601,505)** | |
| Proceeds from stock issued for stock plans and other | **20,672** | 34,376 |
| **Net Cash Provided (Used) by Financing Activities of Continuing Operations** | **(313,578)** | 26,729 |
| **Effect of Exchange Rate Changes on Cash** | **(2,725)** | 5,334 |
| **Net Change in Cash and Cash Equivalents** | **141,234** | (151,179) |
| **Cash and Cash Equivalents Beginning of Period** | **323,203** | 434,191 |

| | | |
|---|---|---|
| **Cash and Cash Equivalents End of Period** | **$ 464,437** | $ 283,012 |

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

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

## Note 1 Interim Condensed Consolidated Financial Statements

### Basis of Presentation

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

We consistently applied the accounting policies described in our 2007 Annual Report to Stockholders in preparing these unaudited interim financial statements, except for the adoption of FIN 48, Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109 and FIN 48-1, Definition of Settlement in FASB Interpretation No 48 as discussed below. We made all adjustments that are necessary, in our opinion, for a fair statement of the results for the interim periods. These adjustments are of a normal recurring nature. We condensed or omitted from these interim financial statements several notes and other information included in our 2007 Annual Report to Stockholders. You should read these unaudited interim condensed consolidated financial statements in conjunction with our consolidated financial statements presented in our 2007 Annual Report to Stockholders.

### Recently Issued Accounting Pronouncements

In June 2007, the Emerging Issues Task Force ( EITF ) reached a consensus on Issue No. 06-11, Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards. EITF 06-11 states that an entity should recognize a realized tax benefit associated with dividends or dividend equivalents on nonvested equity shares, nonvested equity share units, and outstanding equity share options charged to retained earnings as an increase in capital in excess of par value. The amount recognized in capital in excess of par value should be included in the pool of excess tax benefits available to absorb potential future tax deficiencies on share-based payment awards. EITF 06-11 should be applied prospectively to income tax benefits of dividends on equity-classified share-based payment awards that are declared in fiscal years beginning after December 15, 2007. The provisions of EITF 06-11 are effective for our 2009 fiscal year beginning July 1, 2008. We are currently evaluating the provisions of EITF 06-11 and the resulting impact of adoption on our financial statements.

### Adoption of FIN 48

We adopted the provisions of FIN 48, Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109 and FIN 48-1, Definition of Settlement in FASB Interpretation No 48 on July 1, 2007. FIN 48 addresses the recognition and measurement of uncertain income tax positions using a more-likely-than-not threshold and also requires enhanced disclosures in the financial statements. FIN 48-1 amends FIN 48 to provide guidance on how companies should determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits.

As a result of our adoption, we recognized a $36.7 million increase in our opening retained earnings relating to our uncertain tax positions. The total amount of unrecognized tax benefits at July 1, 2007 was $67.9 million, of which $33.3 million would affect the effective tax rate if recognized. We recognize interest and penalties related to uncertain tax positions in our provision for income taxes. Although our tax filings are under continual examination by the tax authorities and we regularly assess our tax uncertainties, tax examinations are inherently uncertain. We are unaware of any material tax settlements expected within the next twelve months.

The U.S. statutes of limitation are open for the fiscal tax years 2004 forward. Our major foreign jurisdictions are subject to examination for the tax years 2002 forward. Due to the complex and uncertain examination process, the resolution of such examinations could have a material impact on our results of operations.

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

**Note 2 Events Impacting Comparability**

We are providing the following information on some actions taken by us or events that occurred in the periods indicated:

| Income/(charge) (Dollar amounts in millions) | Three months ended September 30, **2007** | 2006 |
|---|---|---|
| Other charges | **$ -** | $ (3.5) |
| Total employee-related charges, asset impairments and other | **$ -** | $ (3.5) |
| Other events impacting comparability: | | |
| Asset dispositions and legal settlements | **$ 7.6** | $ (9.1) |
| Acquired research and development | | (114.3) |
| Tax items | **(1.8)** | 8.8 |

**Employee-Related Charges, Asset Impairments and Other**

The following items have been recorded in the condensed consolidated statements of operations in employee-related charges, asset impairments and other, except as noted.

*Celera group*

Fiscal 2007

During the fourth quarter of fiscal 2007, the Celera group recorded a pre-tax charge of $0.5 million for severance costs for approximately 20 employees. The charge resulted from a reduction in the Celera group s proteomics-based activities. All of the affected employees were notified as of June 30, 2007, and were terminated by October 31, 2007. During the first quarter of fiscal 2008, we made cash payments of $0.4 million related to this charge. Cash expenditures were funded by available cash. The remaining cash expenditures of $0.1 million are expected to be paid in the second quarter of fiscal 2008.

During the first quarter of fiscal 2007, the Celera group recorded a pre-tax charge of $3.5 million for its estimated share of a damage award in continuing litigation between Abbott Laboratories, our alliance partner, and Innogenetics N.V. In September 2006, a jury found that the sale of hepatitis C virus ( HCV ) genotyping analyte specific reagents ( ASRs ) products by Abbott willfully infringed a U.S. patent owned by Innogenetics and awarded Innogenetics $7.0 million in damages. In January 2007, the U.S. District Court for the Western District of Wisconsin ruled in favor of Innogenetics request for a permanent injunction, and as such, ordered Abbott to withdraw its products from the market. The

Court also reversed the jury verdict of willful infringement and ruled that Abbott did not willfully infringe Innogenetics patent and denied Innogenetics request for enhanced damages and attorneys fees. Innogenetics did not name the Celera group as a party in this lawsuit, but the Celera group has an interest in these products and in the outcome of the litigation because the enjoined products are manufactured by the Celera group and sold through its alliance with Abbott. Also, as these products are part of its alliance with Abbott, the Celera group has agreed to share the cost of this litigation, including the damage award described above. Abbott is appealing the judgment as both Abbott and the Celera group believe that Innogenetics patent is invalid and that the alliance s HCV genotyping ASRs do not infringe Innogenetics patent. On March 8, 2007, the Court of Appeals for the Federal Circuit issued an order denying Abbott s motion for a stay of the permanent injunction during the appeal process, and the alliance therefore will not receive any revenues from the sale of these HCV genotyping products for the foreseeable future. We believe the appeal process may take six months or more to conclude.

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

Charges prior to fiscal 2007

During fiscal 2006, the Celera group recorded pre-tax charges of $26.4 million related to its decision to exit its small molecule drug discovery and development programs and the integration of Celera Diagnostics into the Celera group. These charges consisted of $12.8 million of employee-related charges, $9.8 million of asset impairments, $1.2 million of excess lease space, and $2.6 million of other disposal costs. The remaining required cash expenditures of $0.9 million as of September 30, 2007, the majority of which related to the asset impairment of an owned facility, are expected to be disbursed by December 31, 2007.

During the first three months of fiscal 2008, the Celera group made net cash payments of approximately $0.2 million related to an excess facility lease space charge for our discontinued Paracel business that was recorded in fiscal 2005. The remaining net cash expenditures of approximately $2.5 million as of September 30, 2007 related to this charge are expected to be disbursed by fiscal 2011.

*Applied Biosystems group*

Charges prior to fiscal 2007

During the first three months of fiscal 2008, the Applied Biosystems group made cash payments of approximately $0.4 million related to excess facility lease space charges recorded in fiscal 2005. The remaining cash payments of $0.2 million as of September 30, 2007 are expected to be disbursed by fiscal 2011.

**Other Events Impacting Comparability**

*Asset dispositions and legal settlements*

The following items have been recorded in the condensed consolidated statements of operations in asset dispositions and legal settlements.

Fiscal 2008

In the first quarter of fiscal 2008, the Applied Biosystems group recorded a $7.6 million pre-tax gain primarily related to a settlement and licensing agreement entered into with Stratagene Corporation and Agilent Technologies, Inc. (which acquired Stratagene), which resolved outstanding legal disputes with Stratagene.

Fiscal 2007

In the first quarter of fiscal 2007, the Applied Biosystems group recorded a $9.1 million pre-tax charge related to a settlement agreement entered into with another company which resolved outstanding legal disputes with that company.

*Acquired research and development*

In the first quarter of fiscal 2007, the Applied Biosystems group recorded a $114.3 million charge to write off the value of acquired in-process research and development ( IPR&D ) in connection with the acquisition of Agencourt Personal Genomics, Inc. ( APG ). As of the acquisition date, the technological feasibility of the acquired project had not been established, and it was determined that the acquired project had no future alternative use. The determination of the amount attributed to acquired IPR&D took into consideration an independent appraisal performed by an outside consultant.

*Tax items*

Fiscal 2008

In the first quarter of fiscal 2008, the Applied Biosystems group recorded tax charges of $1.8 million primarily related to the recalculation of deferred tax assets as a result of a decrease in the statutory tax rate in Germany.

Fiscal 2007

In the first quarter of fiscal 2007, the Applied Biosystems group recorded a tax benefit of $8.8 million related to a reduction in the valuation allowance for German net operating loss carryforwards.

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

## Note 3 Acquisitions subsequent to September 30, 2007

In September 2007, we signed a definitive agreement to acquire Berkeley HeartLab, Inc. ( BHL ) for approximately $195 million in cash. The acquisition of BHL was completed on October 12, 2007. BHL, with operations in Burlingame and Alameda, California, is a cardiovascular healthcare company with a broad portfolio of Clinical Laboratory Improvement Amendments ( CLIA ) certified tests and disease management services focused on the secondary prevention market. We believe that the acquisition will provide the Celera group with a commercial infrastructure to bring its new genetic tests to the American cardiovascular market. Additionally, BHL is expected to provide opportunities for the Celera group to commercialize new tests and technologies and to gain economies of scale and improve its margins as a consequence of the vertical integration with BHL s laboratory service business. The net assets and results of operations of BHL will be allocated to the Celera group.

Also in September 2007, we signed a definitive agreement to acquire substantially all of the assets of Atria Genetics, Inc., a privately held company based in South San Francisco, CA, for approximately $33 million in cash. The acquisition of Atria was completed on October 23, 2007. Atria has a line of human leukocyte antigen ( HLA ) testing products that are used for identifying potential donors in the matching process for bone marrow transplantation. With this acquisition, the Celera group is expected to retain 60 percent of the end-user revenues under its current distribution agreement with Abbott, and also continue to receive a low single digit percentage royalty on the total end-user revenues. The net assets and results of operations of Atria will be allocated to the Celera group.

## Note 4 Earnings (Loss) per Share

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

| | Applied Biosystems Group | | Celera Group | |
|---|---|---|---|---|
| (Dollar amounts in millions, except per share amounts) | **2007** | 2006 | **2007** | 2006 |
| Net income (loss) | **$ 60.9** | $(58.7) | **$ 0.7** | $ (7.1) |
| Allocated intercompany sale of assets | | (0.1) | | |
| Allocated interperiod taxes | **0.1** | (0.1) | | |
| Total net income (loss) allocated | **61.0** | (58.9) | **0.7** | (7.1) |
| Less dividends declared on common stock | **7.8** | 7.7 | | |
| Undistributed earnings (loss) | **$ 53.2** | $(66.6) | **$ 0.7** | $ (7.1) |
| **Allocation of basic earnings (loss) per share** | | | | |
| Basic distributed earnings per share | **$ 0.04** | NA* | **$ -** | $ - |
| Basic undistributed earnings (loss) per share | **0.29** | NA* | **0.01** | (0.09) |
| Total basic earnings (loss) per share | **$ 0.33** | $(0.32) | **$0.01** | $ (0.09) |
| **Allocation of diluted earnings (loss) per share** | | | | |
| Diluted distributed earnings per share | **$ 0.04** | NA* | **$ -** | $ - |
| Diluted undistributed earnings (loss) per share | **0.28** | NA* | **0.01** | (0.09) |
| Total diluted earnings (loss) per share | **$ 0.32** | $(0.32) | **$0.01** | $ (0.09) |
| **Weighted average number of common shares** | | | | |

| | | | | |
|---|---|---|---|---|
| Basic | **183.0** | 182.1 | **79.1** | 77.8 |
| Common stock equivalents | **5.4** | | **1.3** | |
| Diluted | **188.4** | 182.1 | **80.4** | 77.8 |

* Due to the net loss incurred for the first three months ended September 30, 2006, undistributed earnings per share have not been presented. Dividends for the three months ended September 30, 2006 were distributed from prior periods earnings.

Options to purchase shares at exercise prices greater than the average market prices of our two classes of common stock were excluded from the computation of diluted earnings per share because the effect was antidilutive. Additionally, for

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

the three months ended September 30, 2006, options to purchase shares of both Applera Corporation-Applied Biosystems Group Common Stock ( Applera-Applied Biosystems Stock ) and Applera Corporation-Celera Group Common Stock ( Applera-Celera stock ) were excluded from the computation of diluted loss per share because the effect was antidilutive. The following table presents the number of shares excluded from the diluted earnings and loss per share computations at September 30:

| (Shares in millions) | **2007** | 2006 |
|---|---|---|
| Applera-Applied Biosystems stock | **6.1** | 5.1 |
| Applera-Celera stock | **2.6** | 7.1 |

**Note 5 Comprehensive Gain (Loss)**

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

| | Three months ended September 30, | |
|---|---|---|
| (Dollar amounts in millions) | **2007** | 2006 |
| Net income (loss) | **$61.7** | $(66.0) |
| Other comprehensive gain (loss): | | |
| Net unrealized gains (losses) on investments | **(0.6)** | 2.1 |
| Net unrealized (gains) losses on investments reclassified into earnings | **0.2** | (0.2) |
| Net unrealized gains (losses) on hedge contracts | **(9.8)** | 2.0 |
| Net unrealized gains on hedge contracts reclassified into earnings | **(0.5)** | |
| Foreign currency translation adjustments | **13.8** | 2.5 |
| Pension and postretirement benefits | **0.6** | |
| Total other comprehensive gain | **3.7** | 6.4 |
| Total comprehensive gain (loss) | **$65.4** | $(59.6) |

**Note 6 Inventories**

Inventories included the following components:

| (Dollar amounts in millions) | **September 30, 2007** | June 30, 2007 |
|---|---|---|
| Raw materials and supplies | **$ 52.5** | $ 49.9 |
| Work-in-process | **9.7** | 6.3 |

| | | |
|---|---|---|
| Finished products | **95.7** | 84.1 |
| Total inventories, net | **$157.9** | $140.3 |

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

**Note 7 Goodwill and Intangible Assets**

The carrying amounts of our intangible assets were as follows:

| | **September 30, 2007** | | June 30, 2007 | |
|---|---|---|---|---|
| (Dollar amounts in millions) | Gross Carrying Amount | Accumulated Amortization | Gross Carrying Amount | Accumulated Amortization |
| **Amortized intangible assets** | | | | |
| Acquired technology | **$ 85.9** | **$60.0** | $ 83.7 | $57.4 |
| Patents | **29.9** | **25.5** | 29.9 | 25.1 |
| Customer relationships | **27.1** | **6.1** | 27.1 | 5.2 |
| Other | **1.7** | **0.8** | 1.7 | 0.7 |
| Total amortized intangible assets | **$144.6** | **$92.4** | $142.4 | $88.4 |
| **Unamortized intangible assets** | | | | |
| Trade name | **4.9** | | 4.9 | |
| Total | **$149.5** | **$92.4** | $147.3 | $88.4 |

Aggregate amortization expense was as follows:

| | Three months ended September 30, | |
|---|---|---|
| (Dollar amounts in millions) | **2007** | 2006 |
| Applied Biosystems group | **$3.6** | $4.4 |
| Celera group | **0.4** | 0.6 |
| Consolidated | **$4.0** | $5.0 |

We record amortization expense in cost of sales, except for amortization of acquisition-related intangible assets which is recorded in the amortization of purchased intangible assets in the condensed consolidated statements of operations. At September 30, 2007, we estimated annual amortization expense of our intangible assets for each of the next five fiscal years as shown in the following table. Future acquisitions or impairment events could cause these amounts to change.

| (Dollar amounts in millions) | Applied Biosystems Group | Celera Group | Consolidated |
|---|---|---|---|

| | | | |
|---|---|---|---|
| Remainder of fiscal 2008 | **$10.5** | **$0.1** | **$10.6** |
| 2009 | **13.3** | **0.2** | **13.5** |
| 2010 | **10.8** | **0.2** | **11.0** |
| 2011 | **6.9** | **0.1** | **7.0** |
| 2012 | **5.7** | | **5.7** |

The carrying amount of goodwill at September 30, 2007 and June 30, 2007, was $245.9 million, of which $243.2 million was allocated to the Applied Biosystems group and $2.7 million was allocated to the Celera group.

**Note 8 Debt and Lines of Credit**

We maintain a $250 million unsecured revolving credit agreement with four banks that matures on May 25, 2012. This amount was increased from $200 million effective August 27, 2007, at our request in accordance with the terms of the agreement. Borrowings under this agreement may be made in U.S. dollars and other currencies, and bear interest at a fluctuating rate generally equal to Citibank, N.A. s base rate or at a periodic fixed rate equal to LIBOR plus a margin of between 15 and 32.5 basis points based on our long-term senior unsecured non-credit enhanced debt ratings.

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APPLERA CORPORATION

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

Commitment and facility fees are also based on our long-term senior unsecured non-credit enhanced debt ratings. As of September 30, 2007, there was $175 million outstanding under this agreement, classified as loans payable in the condensed consolidated statement of financial position. There were no borrowings outstanding under this agreement at June 30, 2007.

On August 27, 2007, we entered into a $100 million unsecured term loan agreement with Bank of America, N.A. that matures on September 4, 2008. Upon the satisfaction of various conditions, we have the option to extend the maturity date on this agreement to September 4, 2010. If we exercise this option, we would then be required to make partial repayments each quarter, commencing after the original maturity date, equal to 3 percent of the original principal amount of the loan. Borrowings under this agreement bear interest at a fluctuating rate generally equal to Bank of America, N.A. s base rate or at a periodic fixed rate equal to LIBOR plus a margin of between 20 and 40 basis points based on our long-term senior unsecured non-credit enhanced debt ratings. There was $100 million outstanding under this agreement, classified as loans payable in the condensed consolidated statement of financial position, at September 30, 2007.

Both the revolving credit agreement and the term loan agreement require that we maintain a debt to total capital ratio, as defined in each agreement, of not more than 0.50:1:00.

The amounts borrowed under these agreements were used to fund the repurchase of shares of Applera-Applied Biosystems group stock and were allocated entirely to the Applied Biosystems group. In August 2007, we entered into an agreement with Morgan Stanley & Co. Incorporated for the accelerated repurchase of $600 million of the Applied Biosystems group s common stock. During the first quarter of fiscal 2008, we paid Morgan Stanley approximately $602 million for this transaction, of which $275 million was funded by loans payable and the balance with cash.

The weighted average interest rate on all amounts outstanding under these agreements at September 30, 2007 was 5.80%.

**Note 9 Supplemental Cash Flow Information**

Significant non-cash financing activity for the three months ended September 30 was as follows:

| (Dollar amounts in millions) | **2007** | 2006 |
|---|---|---|
| Dividends declared but not paid | **$7.8** | $7.7 |
| Tax benefit related to employee stock options | **3.7** | 4.8 |

**Note 10 Guarantees**

**Leases**

We provide lease-financing options to our customers through third party financing companies. For some leases, the financing companies have recourse to us for any unpaid principal balance on default by the customer. The leases typically have terms of two to three years and are secured by the underlying instrument. In the event of default by a customer, we would repossess the underlying instrument. We record revenues from these transactions on the completion of installation and acceptance of products and maintain a reserve for estimated losses on all lease transactions with recourse provisions based on historical default rates and current economic conditions. At September 30, 2007, the financing companies outstanding balance of lease receivables with recourse to us was $5.2 million. We believe that we could recover the entire balance from the resale of the underlying instruments in the event of default by all customers.

**Pension Benefits**

As part of the divestiture of our Analytical Instruments business in fiscal 1999, the purchaser of the Analytical Instruments business is paying for the pension benefits for employees of a former German subsidiary. However, we guaranteed payment of these pension benefits should the purchaser fail to do so, as these payment obligations were not transferable to the buyer under German law. The guaranteed payment obligation, which approximated $61.3 million at September 30, 2007, is not expected to have a material adverse effect on our condensed consolidated statement of financial position.

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

**Indemnifications**

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

**Product Warranties**

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

The following table provides an analysis of the warranty reserve for the three months ended September 30:

| (Dollar amounts in millions) | **2007** | 2006 |
|---|---|---|
| Balance beginning of period | **$12.1** | $10.6 |
| Accruals for warranties | **4.2** | 3.4 |
| Usage of reserve | **(5.2)** | (3.8) |
| Other* | **0.9** | (0.1) |
| Balance at September 30 | **$12.0** | $10.1 |

* Other consists of accrual adjustments to reflect actual experience and currency translation.

**Note 11 Pension and Other Postretirement Benefits**

The components of net pension and postretirement benefit expenses for the three month period ended September 30 were as follows:

| | Three months ended September 30, | |
|---|---|---|
| (Dollar amounts in millions) | **2007** | 2006 |
| **Pension** | | |

| | | |
|---|---|---|
| Service cost | **$ 0.9** | $ 1.0 |
| Interest cost | **11.3** | 10.9 |
| Expected return on plan assets | **(12.3)** | (11.8) |
| Amortization of prior service cost | **0.3** | 0.2 |
| Amortization of losses | **0.7** | 1.2 |
| Net periodic expense | **$ 0.9** | $ 1.5 |
| **Postretirement Benefit** | | |
| Interest cost | **$ 0.7** | $ 0.9 |
| Amortization of gains | | (0.1) |
| Net periodic expense | **$ 0.7** | $ 0.8 |

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

We contributed approximately $0.4 million to our foreign and non-qualified domestic plans during the three months ended September 30, 2007, and expect to contribute an additional $2.0 million during the remainder of fiscal 2008. Based on the level of our contributions to the qualified U.S. pension plan during previous years, combined with the performance of the assets invested in the plan, we do not expect to have to fund our qualified U.S. pension plan in fiscal 2008 in order to meet minimum statutory funding requirements. We made benefit payments of approximately $1.5 million under the postretirement plan during the three months ended September 30, 2007, and we expect to make approximately $4.5 million of additional benefit payments during the remainder of fiscal 2008.

**Note 12 Contingencies**

**Legal Proceedings**

We are involved in various lawsuits, arbitrations, investigations, and other legal actions from time to time with both private parties and governmental entities. These legal actions currently involve, for example, commercial, intellectual property, antitrust, environmental, securities, and employment matters. The following is a description of some claims we are currently defending, including some counterclaims brought against us in response to claims filed by us against others. We believe that we have meritorious defenses against the claims currently asserted against us, including those described below, and intend to defend them vigorously.

The company and some of its officers are defendants in a lawsuit brought on behalf of purchasers of Applera-Celera stock in our follow-on public offering of Applera-Celera stock completed on March 6, 2000. In the offering, we sold an aggregate of approximately 4.4 million shares of Applera-Celera stock at a public offering price of $225 per share. The lawsuit, which was commenced with the filing of several complaints in April and May 2000, is pending in the U.S. District Court for the District of Connecticut, and an amended consolidated complaint was filed on August 21, 2001. The consolidated complaint generally alleges that the prospectus used in connection with the offering was inaccurate or misleading because it failed to adequately disclose the alleged opposition of the Human Genome Project and two of its supporters, the governments of the U.S. and the U.K., to providing patent protection to our genomic-based products. Although the Celera group has never sought, or intended to seek, a patent on the basic human genome sequence data, the complaint also alleges that we did not adequately disclose the risk that the Celera group would not be able to patent this data. The consolidated complaint seeks monetary damages, rescission, costs and expenses, and other relief as the court deems proper. On March 31, 2005, the court certified the case as a class action.

We filed a patent infringement action against Stratagene Corporation in the U.S. District Court for the District of Connecticut on November 9, 2004. The complaint alleged that Stratagene, which was acquired by Agilent Technologies, Inc. since our filing of the action, infringed U.S. Patent No. 6,814,934 because of its activities involving instruments for real-time PCR detection. We were seeking monetary damages, costs, expenses, injunctive relief, and other relief as the court deemed proper. Stratagene answered the complaint and counterclaimed for declaratory relief that the 934 patent was invalid and not infringed. Stratagene was seeking dismissal of our complaint, a judgment that the 934 patent was invalid and not infringed, costs and expenses, and other relief as the court deemed proper. We were involved in similar litigation with Stratagene in Germany, France, and the Netherlands involving European Patent No. 872562, the European counterpart to the 934 patent. On September 18, 2007, we announced that we had entered into a settlement agreement with Stratagene and Agilent that resolved these claims and counterclaims, including the additional litigation in Germany, France, and the Netherlands. Pursuant to the settlement agreement, we have licensed the patents at issue to Stratagene and Agilent. The District Court formally dismissed the case on September 26, 2007, and the legal proceedings in Germany, France, and the Netherlands have also been formally dismissed.

Enzo Biochem, Inc., Enzo Life Sciences, Inc., and Yale University filed a patent infringement action against us in the U.S. District Court for the District of Connecticut on June 8, 2004. The complaint alleges that we are infringing six patents. Four of these patents are assigned to Yale University and licensed exclusively to Enzo Biochem, i.e., U.S. Patent No. 4,476,928, entitled Modified Nucleotides and Polynucleotides and Complexes Formed Therefrom, U.S. Patent No. 5,449,767, entitled Modified Nucleotides and Polynucleotides and Methods of Preparing Same, U.S. Patent No. 5,328,824 entitled Methods of Using Labeled Nucleotides, and U.S. Patent No. 4,711,955, entitled Modified Nucleotides and Polynucleotides and Methods of Preparing and Using Same. These four patents have since expired. The other two patents are assigned to Enzo Life Sciences, i.e., U.S. Patent No. 5,082,830 entitled End Labeled

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

Nucleotide Probe and U.S. Patent No. 4,994,373 entitled Methods and Structures Employing Compoundly Labeled Polynucleotide Probes. The allegedly infringing products include the Applied Biosystems group s sequencing reagent kits, its TaqMan® genotyping and gene expression assays, and the gene expression microarrays used with its Expression Array System. Enzo Biochem, Enzo Life Sciences, and Yale University are seeking monetary damages, costs, expenses, injunctive relief, and other relief as the court deems proper. In August and September, 2007, the court issued a series of orders favorable to Applera and dismissing all of these claims. Enzo immediately filed a Notice of Appeal with the United States Court of Appeals for the Federal Circuit contesting those orders.

Molecular Diagnostics Laboratories filed a class action complaint against us and Hoffmann-La Roche, Inc. in the U.S. District Court for the District of Columbia on September 23, 2004, and filed an amended complaint on July 5, 2006. The amended complaint alleges anticompetitive conduct in connection with the sale of Taq DNA polymerase. The anticompetitive conduct is alleged to arise from the prosecution and enforcement of U.S. Patent No. 4,889,818. This patent is assigned to Hoffmann-La Roche, with whom we have a commercial relationship covering, among other things, this patent and the sale of Taq DNA polymerase. The complaint seeks monetary damages, costs, expenses, injunctive relief, and other relief as the court deems proper. On July 5, 2006, the court certified the case as a class action.

We are involved in several legal actions with Thermo Electron Corporation and its subsidiary Thermo Finnigan LLC. These legal actions commenced when we, together with MDS, Inc. and our Applied Biosystems/MDS SCIEX Instruments joint venture with MDS, filed a patent infringement action against Thermo Electron in the U.S. District Court for the District of Delaware on September 3, 2004. The complaint alleges infringement by Thermo Electron of U.S. Patent No. 4,963,736, and seeks monetary damages, costs, expenses, and other relief as the court deems proper. Thermo Electron has answered the complaint and counterclaimed for declaratory relief that the 736 patent is invalid, not infringed, and unenforceable, and is seeking dismissal of our complaint, a judgment that the 736 patent is invalid, not infringed, and unenforceable, costs and expenses, and other relief as the court deems proper. After the filing of the action against Thermo Electron, on December 8, 2004, Thermo Finnigan filed a patent infringement action against us in the U.S. District Court for the District of Delaware. The complaint alleges that we have infringed U.S. Patent No. 5,385,654 as a result of, for example, our Applied Biosystems group s commercialization of the ABI PRISM® 3700 Genetic Analyzer. Thermo Finnigan is seeking monetary damages, costs, expenses, and other relief as the court deems proper. We have answered the complaint and counterclaimed for declaratory relief that the 654 patent is invalid, not infringed, and unenforceable, and are seeking dismissal of Thermo Finnigan s complaint, a judgment that the 654 patent is invalid, not infringed, and unenforceable, costs and expenses, and other relief as the court deems proper. Thermo Finnigan subsequently filed a second patent infringement action against us, MDS, and the Applied Biosystems/MDS SCIEX Instruments joint venture, in the U.S. District Court for the District of Delaware on February 23, 2005. The complaint alleges that we and the other defendants have infringed U.S. Patent No. 6,528,784 as a result of, for example, our commercialization of the API 5000 LC/MS/MS system. Thermo Finnigan is seeking monetary damages, costs, expenses, and other relief as the court deems proper. We have answered the complaint and counterclaimed for declaratory relief that the 784 patent is invalid and not infringed, and are seeking dismissal of Thermo Finnigan s complaint, a judgment that the 784 patent is invalid and not infringed, costs and expenses, and other relief as the court deems proper.

We are involved in two legal actions with Michigan Diagnostics LLC. These legal actions commenced when we filed a complaint for patent infringement against Michigan Diagnostics on March 26, 2007, in the United States District Court for the District of Massachusetts. We amended the complaint on April 5, 2007. The amended complaint alleges infringement by Michigan Diagnostics of U.S. Patent Nos. 6,514,717, 6,322,727 and 6,107,024, which are related to chemiluminescent products and methods, and seeks monetary damages, costs, expenses, injunctive, and other relief as the court deems proper. Michigan Diagnostics has not yet filed an answer to our complaint. Subsequently, on May 14, 2007, Michigan Diagnostics filed a complaint against Applera in the U.S. District Court for the Eastern District of Michigan. The complaint seeks a declaratory judgment of non-infringement, invalidity, and unenforceability of approximately 60 patents related to chemiluminescent products and methods, and includes antitrust claims based on our alleged misconduct in our alleged enforcement of those patents. The patents asserted by Applera in the Massachusetts case are among those included in the complaint filed by Michigan Diagnostics.

We have not yet filed an answer to this complaint.

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

We filed a complaint on May 31, 2007, in the U.S. District Court for the Northern District of California against Illumina, Inc., Solexa Inc., and a former chief patent counsel to our company, seeking an injunction restoring to us patents and patent applications that were filed by the former chief patent counsel but are on their face assigned to Solexa, which was acquired by Illumina in January 2007. The complaint also seeks a declaration of our rights and duties regarding infringement of these patents, in addition to monetary damages, costs, expenses, and other relief as the court deems proper. We previously filed a related complaint, on December 26, 2006, in the Superior Court of the State of California (Santa Clara County), also seeking restoration of these patents and patent applications to us. Pursuant to a joint stipulation of the parties, the California state court action was dismissed on August 7, 2007. On August 13, 2007, Solexa filed its answer to the federal complaint and counterclaimed that we make, use, sell, and offer for sale DNA sequencing products that infringe the patents, U.S. Patent Nos. 5,750,341, 5,969,119, 6,306,597. Solexa is seeking monetary damages, costs, expenses, injunctive relief, and other relief as the court deems proper.

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

**Note 13 Discontinued Operations**

During the first quarter of fiscal 2008, we received $12.9 million in cash related to the settlement of German tax audits related to one of our former German affiliates.

**Note 14 Segment and Consolidating Information**

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

See Note 16 to our consolidated financial statements included in our 2007 Annual Report to Stockholders for a detailed description of the segments and the management and allocation policies applicable to the attribution of assets, liabilities, revenues and expenses to the segments (which information is incorporated in this quarterly report by reference).

Applied Biosystems group recorded net revenues from leased instruments and sales of consumables and project materials to the Celera group of $0.7 million for the three months ended September 30, 2007 and $1.1 million for the three months ended September 30, 2006.

Additionally, in accordance with our tax allocation policy, the Applied Biosystems group received, without reimbursement to the Celera group, $3.6 million in the first three months of fiscal 2008 and $8.6 million in the first three months of fiscal 2007 some of the tax benefits generated by the Celera group.

In the following consolidating financial information, the Eliminations column represents the elimination of intersegment activity.

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

**Condensed Consolidating Statement of Operations for the Three Months Ended September 30, 2007**

| (Dollar amounts in thousands) | Applied Biosystems Group | Celera Group | Eliminations | Consolidated |
|---|---|---|---|---|
| Products | $405,047 | $ 2,445 | $ - | $407,492 |
| Services | 64,373 | | | 64,373 |
| Other | 31,112 | 13,696 | | 44,808 |
| Net revenues from external customers | 500,532 | 16,141 | - | 516,673 |
| Intersegment revenues | 714 | | (714) | |
| **Total Net Revenues** | 501,246 | 16,141 | (714) | 516,673 |
| Products | 189,666 | 3,091 | (178) | 192,579 |
| Services | 28,801 | | (54) | 28,747 |
| Other | 2,839 | 62 | | 2,901 |
| **Cost of Sales** | 221,306 | 3,153 | (232) | 224,227 |
| **Gross Margin** | 279,940 | 12,988 | (482) | 292,446 |
| Selling, general and administrative | 148,432 | 8,068 | (6) | 156,494 |
| Research and development | 50,547 | 10,721 | (459) | 60,809 |
| Amortization of purchased intangible assets | 2,612 | | | 2,612 |
| Asset dispositions and legal settlements | (7,556) | | | (7,556) |
| **Operating Income (Loss)** | 85,905 | (5,801) | (17) | 80,087 |
| Interest income, net | 3,680 | 7,133 | | 10,813 |
| Other income (expense), net | 1,070 | (283) | | 787 |
| **Income before Income Taxes** | 90,655 | 1,049 | (17) | 91,687 |
| Provision for income taxes | 29,713 | 384 | (100) | 29,997 |
| **Net Income** | $ 60,942 | $ 665 | $ 83 | $ 61,690 |

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

**Condensed Consolidating Statement of Financial Position at September 30, 2007**

| (Dollar amounts in thousands) | Applied Biosystems Group | Celera Group | Eliminations | Consolidated |
|---|---|---|---|---|
| **Assets** | | | | |
| Current assets | | | | |
| Cash and cash equivalents | $ 277,176 | $187,261 | $ - | $ 464,437 |
| Short-term investments | | 360,874 | | 360,874 |
| Accounts receivable, net | 414,089 | 16,494 | (454) | 430,129 |
| Inventories, net | 148,766 | 9,708 | (596) | 157,878 |
| Prepaid expenses and other current assets | 144,031 | 31,786 | (1,965) | 173,852 |
| Total current assets | 984,062 | 606,123 | (3,015) | 1,587,170 |
| Property, plant and equipment, net | 379,970 | 6,572 | (161) | 386,381 |
| Goodwill and intangible assets, net | 299,755 | 3,255 | | 303,010 |
| Other long-term assets | 467,457 | 168,270 | 335 | 636,062 |
| **Total Assets** | $2,131,244 | $784,220 | $(2,841) | $2,912,623 |
| | | | | |
| **Liabilities and Stockholders Equity** | | | | |
| Current liabilities | | | | |
| Loans payable | $ 275,000 | $ - | $ - | $ 275,000 |
| Accounts payable | 153,217 | 2,598 | (2,023) | 153,792 |
| Accrued salaries and wages | 56,730 | 3,421 | | 60,151 |
| Current deferred tax liability | 16,149 | | | 16,149 |
| Accrued taxes on income | 16,992 | 65 | | 17,057 |
| Other accrued expenses | 272,038 | 10,349 | (556) | 281,831 |
| Total current liabilities | 790,126 | 16,433 | (2,579) | 803,980 |
| Other long-term liabilities | 264,663 | 4,849 | (169) | 269,343 |
| **Total Liabilities** | 1,054,789 | 21,282 | (2,748) | 1,073,323 |
| | | | | |
| **Total Stockholders Equity** | 1,076,455 | 762,938 | (93) | 1,839,300 |
| **Total Liabilities and Stockholders Equity** | $2,131,244 | $784,220 | $(2,841) | $2,912,623 |

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

**Condensed Consolidating Statement of Cash Flows for the Three Months Ended September 30, 2007**

| (Dollar amounts in thousands) | Applied Biosystems Group | Celera Group | Eliminations | Consolidated |
|---|---|---|---|---|
| **Operating Activities of Continuing Operations** | | | | |
| Net income | $ 60,942 | $ 665 | $ 83 | $ 61,690 |
| Adjustments to reconcile net income to net cash provided (used) by operating activities: | | | | |
| Depreciation and amortization | 18,604 | 1,499 | (78) | 20,025 |
| Share-based compensation and pension | 5,900 | 1,101 | | 7,001 |
| Deferred income taxes | 15,099 | 5,458 | (280) | 20,277 |
| Nonreimbursable utilization of intergroup tax benefits | 3,603 | (3,603) | | |
| Changes in operating assets and liabilities: | | | | |
| Accounts receivable | 47,502 | (10,236) | 236 | 37,502 |
| Inventories | (16,296) | (882) | 25 | (17,153) |
| Prepaid expenses and other assets | 12,483 | (1,382) | (58) | 11,043 |
| Accounts payable and other liabilities | (50,703) | (6,953) | 3 | (57,653) |
| **Net Cash Provided (Used) by Operating Activities of Continuing Operations** | 97,134 | (14,333) | (69) | 82,732 |
| **Net Cash Provided by Discontinued Operations** | 12,900 | | | 12,900 |
| **Investing Activities of Continuing Operations** | | | | |
| Additions to property, plant and equipment, net | (9,514) | (313) | 69 | (9,758) |
| Proceeds from maturities of available-for-sale investments | | 30,409 | | 30,409 |
| Proceeds from sales of available-for-sale investments | 213,850 | 182,842 | | 396,692 |
| Purchases of available-for-sale investments | (12,553) | (42,706) | | (55,259) |
| Acquisitions and investments | (179) | | | (179) |
| **Net Cash Provided by Investing Activities of Continuing Operations** | 191,604 | 170,232 | 69 | 361,905 |
| **Financing Activities** | | | | |
| Proceeds from loans payable | 275,000 | | | 275,000 |
| Dividends | (7,745) | | | (7,745) |
| Purchases of common stock for treasury | (601,505) | | | (601,505) |
| Proceeds from stock issued for stock plans and other | 19,346 | 1,326 | | 20,672 |
| **Net Cash Provided (Used) by Financing Activities of Continuing Operations** | (314,904) | 1,326 | | (313,578) |
| **Effect of Exchange Rate Changes on Cash** | (2,725) | | | (2,725) |
| **Net Change in Cash and Cash Equivalents** | (15,991) | 157,225 | | 141,234 |
| **Cash and Cash Equivalents Beginning of Period** | 293,167 | 30,036 | | 323,203 |
| **Cash and Cash Equivalents End of Period** | $ 277,176 | $187,261 | $ - | $464,437 |

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**APPLERA CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**continued**

**Condensed Consolidating Statement of Operations for the Three Months Ended September 30, 2006**

| (Dollar amounts in thousands) | Applied Biosystems Group | Celera Group | Eliminations | Consolidated |
|---|---|---|---|---|
| Products | $388,596 | $ 2,486 | $ - | $391,082 |
| Services | 58,140 | | | 58,140 |
| Other | 28,444 | 7,743 | | 36,187 |
| Net revenues from external customers | 475,180 | 10,229 | - | 485,409 |
| Intersegment revenues | 1,093 | | (1,093) | |
| **Total Net Revenues** | 476,273 | 10,229 | (1,093) | 485,409 |
| Products | 193,376 | 3,644 | (361) | 196,659 |
| Services | 24,669 | | (71) | 24,598 |
| Other | 2,670 | 157 | | 2,827 |
| **Total Cost of Sales** | 220,715 | 3,801 | (432) | 224,084 |
| **Gross Margin** | 255,558 | 6,428 | (661) | 261,325 |
| Selling, general and administrative | 123,545 | 5,647 | 13,193 | 142,385 |
| Corporate allocated expenses | 11,605 | 1,594 | (13,199) | |
| Research and development | 45,115 | 13,221 | (434) | 57,902 |
| Amortization of purchased intangible assets | 2,737 | | | 2,737 |
| Employee-related charges, asset impairments and other | | 3,500 | | 3,500 |
| Asset dispositions and legal settlements | 9,087 | | | 9,087 |
| Acquired research and development | 114,251 | | | 114,251 |
| **Operating Loss** | (50,782) | (17,534) | (221) | (68,537) |
| Gain on investments, net | 209 | | | 209 |
| Interest income, net | 2,630 | 6,583 | | 9,213 |
| Other income (expense), net | 1,314 | 103 | | 1,417 |
| **Loss before Income Taxes** | (46,629) | (10,848) | (221) | (57,698) |
| Provision (benefit) for income taxes | 12,093 | (3,797) | 18 | 8,314 |
| **Net Loss** | $ (58,722) | $ (7,051) | $ (239) | $ (66,012) |

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APPLERA CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

continued

**Condensed Consolidating Statement of Financial Position at June 30, 2007**

| (Dollar amounts in thousands) | Applied Biosystems Group | Celera Group | Eliminations | Consolidated |
|---|---|---|---|---|
| **Assets** | | | | |
| Current assets | | | | |
| Cash and cash equivalents | $ 293,167 | $ 30,036 | $ - | $ 323,203 |
| Short-term investments | 201,297 | 531,460 | | 732,757 |
| Accounts receivable, net | 446,833 | 6,258 | (218) | 452,873 |
| Inventories, net | 132,094 | 8,826 | (571) | 140,349 |
| Prepaid expenses and other current assets | 161,040 | 30,360 | (1,995) | 189,405 |
| Total current assets | 1,234,431 | 606,940 | (2,784) | 1,838,587 |
| Property, plant and equipment, net | 383,594 | 7,386 | (170) | 390,810 |
| Goodwill and intangible assets, net | 301,138 | 3,674 | | 304,812 |
| Other long-term assets | 467,441 | 150,683 | 207 | 618,331 |
| **Total Assets** | $2,386,604 | $768,683 | $(2,747) | $3,152,540 |
| | | | | |
| **Liabilities and Stockholders Equity** | | | | |
| Current liabilities | | | | |
| Accounts payable | $ 161,440 | $ 3,016 | $(1,791) | $ 162,665 |
| Accrued salaries and wages | 99,694 | 8,858 | | 108,552 |
| Current deferred tax liability | 15,633 | | | 15,633 |
| Accrued taxes on income | 51,212 | 15,489 | | 66,701 |
| Other accrued expenses | 259,743 | 10,463 | (583) | 269,623 |
| Total current liabilities | 587,722 | 37,826 | (2,374) | 623,174 |
| Other long-term liabilities | 208,550 | 4,959 | (197) | 213,312 |
| **Total Liabilities** | 796,272 | 42,785 | (2,571) | 836,486 |
| | | | | |
| **Total Stockholders Equity** | 1,590,332 | 725,898 | (176) | 2,316,054 |
| **Total Liabilities and Stockholders Equity** | $2,386,604 | $768,683 | $(2,747) | $3,152,540 |

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APPLERA CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

continued

**Condensed Consolidating Statement of Cash Flows for the Three Months Ended September 30, 2006**

| (Dollar amounts in thousands) | Applied Biosystems Group | Celera Group | Eliminations | Consolidated |
|---|---|---|---|---|
| **Operating Activities** | | | | |
| Net loss | $ (58,722) | $ (7,051) | $ (239) | $ (66,012) |
| Adjustments to reconcile net loss to net cash provided (used) by operating activities: | | | | |
| Depreciation and amortization | 19,376 | 1,781 | (78) | 21,079 |
| Employee-related charges and other | | 3,500 | | 3,500 |
| Share-based compensation programs | 3,728 | 775 | | 4,503 |
| Deferred income taxes | (7,409) | 4,631 | (892) | (3,670) |
| Sale of assets and legal settlements, net | (209) | | | (209) |
| Acquired research and development | 114,251 | | | 114,251 |
| Nonreimbursable utilization of intergroup tax benefits | 8,563 | (8,563) | | |
| Changes in operating assets and liabilities: | | | | |
| Accounts receivable | 38,249 | 3,167 | 94 | 41,510 |
| Inventories | (5,234) | (138) | 233 | (5,139) |
| Prepaid expenses and other assets | (11,304) | (1,574) | (3,403) | (16,281) |
| Accounts payable and other liabilities | (78,319) | (10,793) | 4,245 | (84,867) |
| **Net Cash Provided (Used) by Operating Activities** | 22,970 | (14,265) | (40) | 8,665 |
| **Investing Activities** | | | | |
| Additions to property, plant and equipment, net | (14,507) | (444) | 40 | (14,911) |
| Proceeds from maturities of available-for-sale investments | | 40,870 | | 40,870 |
| Proceeds from sales of available-for-sale investments | 2,422 | 113,378 | | 115,800 |
| Purchases of available-for-sale investments | (23,878) | (188,707) | | (212,585) |
| Acquisitions and investments | (121,403) | | | (121,403) |
| Proceeds from the sale of assets, net | 322 | | | 322 |
| **Net Cash Used by Investing Activities** | (157,044) | (34,903) | 40 | (191,907) |
| **Financing Activities** | | | | |
| Dividends | (7,647) | | | (7,647) |
| Proceeds from stock issued for stock plans and other | 25,148 | 9,228 | | 34,376 |
| **Net Cash Provided by Financing Activities** | 17,501 | 9,228 | | 26,729 |
| **Effect of Exchange Rate Changes on Cash** | 5,334 | | | 5,334 |
| **Net Change in Cash and Cash Equivalents** | (111,239) | (39,940) | | (151,179) |
| **Cash and Cash Equivalents Beginning of Period** | 373,921 | 60,270 | | 434,191 |
| **Cash and Cash Equivalents End of Period** | $ 262,682 | $ 20,330 | $ - | $ 283,012 |

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**Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations.**

**APPLERA CORPORATION**

**MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The purpose of the following management s discussion and analysis is to provide an overview of the business of Applera Corporation to help facilitate an understanding of significant factors influencing our historical operating results, financial condition, and cash flows and also to convey our expectations of the potential impact of known trends, events, or uncertainties that may impact our future results. You should read this discussion in conjunction with our consolidated financial statements and related notes included in this report and in our 2007 Annual Report to Stockholders. Historical results and percentage relationships are not necessarily indicative of operating results for future periods. When used in this management discussion, the terms Applera, Company, we, us, or our mean Applera Corporation and its subsidiaries.

We have reclassified some prior year amounts for comparative purposes.

**Overview**

We conduct business through two business segments: the Applied Biosystems group and the Celera group.

The Applied Biosystems group serves the life science industry and research community by developing and marketing instrument-based systems, consumables, software, and services. Its customers use these tools to analyze nucleic acids (DNA and RNA), small molecules, and proteins to make scientific discoveries and develop new pharmaceuticals. The Applied Biosystems group s products also serve the needs of some markets outside of life science research, which we refer to as applied markets, such as the fields of: human identity testing (forensic and paternity testing); biosecurity, which refers to products needed in response to the threat of biological terrorism and other malicious, accidental, and natural biological dangers; and quality and safety testing, such as testing required for food and pharmaceutical manufacturing.

The Celera group is a diagnostics business delivering personalized disease management solutions through a combination of tests and services based on proprietary genetics discovery platforms. The business is developing diagnostic products that predict disease risk, and optimize therapy selection and patient outcomes, based on the discovery and validation of novel markers in complex diseases such as cardiovascular disease, breast cancer, and liver and autoimmune diseases. The Celera group also maintains a strategic alliance with Abbott Laboratories for the development and commercialization of some of its molecular diagnostic products.

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

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

Corporation-Celera Group Common Stock ( Applera-Celera stock ) is listed on the New York Stock Exchange under the ticker symbol CRA and is intended to reflect the relative performance of the Celera group. There is no single security that represents the performance of Applera as a whole.

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

On August 8, 2007, we announced that our board of directors has retained Morgan Stanley & Co. Incorporated to explore alternatives to our current tracking stock structure, including the possibility of creating independent publicly-traded companies in place of our two business groups, the Applied Biosystems group and the Celera group. While a final decision has not been made related to this complex analysis, efforts to-date indicate a preference toward dissolving the current structure and creating separate publicly traded companies for the Applied Biosystems group and the Celera group. We intend to update shareholders as the analysis is completed and the decision is finalized.

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APPLERA CORPORATION

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF

OPERATIONS continued

No assurances can be given that the board will ultimately authorize such a transaction or that, if authorized, such a transaction will be consummated.

More information about the risks relating to our capital structure, particularly our two classes of capital stock, is contained in our Annual Report on Form 10-K for fiscal 2007 filed with the Securities and Exchange Commission.

Our fiscal year ends on June 30. The financial information for both segments is presented in Note 14 to our condensed consolidated financial statements, Segment and Consolidating Information. Management s discussion and analysis addresses the consolidated financial results followed by the discussions of our two segments.

**Business Developments:**

Listed below are significant business developments since the filing of our Annual Report on Form 10-K for fiscal 2007.

*Applied Biosystems Group*

- In October 2007, the Applied Biosystems group announced the formal commercial launch of the SOLiD next-generation DNA sequencing system, following an accelerated development program and positive feedback from early-access customers.
- In August 2007, we announced that the board of directors increased to $1.2 billion the current authorization to repurchase shares of Applera Corporation-Applied Biosystems Group stock. Pursuant to the authorization, we executed a $600 million accelerated share repurchase transaction with Morgan Stanley and 16 million shares, or approximately 8.7% of the outstanding shares, were delivered to us during the second quarter of fiscal 2008.

*Celera Group*

- In October 2007, the Celera group completed the acquisition of substantially all of the assets of Atria Genetics, Inc., for approximately $33 million in cash. Atria markets human leukocyte antigen ( HLA ) testing products that are used to match donors and recipients for bone marrow transplantation.

- Also in October, the Celera group completed the acquisition of Berkeley HeartLab, Inc. ( BHL ) for approximately $195 million in cash. BHL is a cardiovascular healthcare company with a broad portfolio of Clinical Laboratory Improvement Amendments ( CLIA ) certified tests and disease management services focused on the secondary prevention market.

- In September 2007, the Celera group announced it entered into agreements with Siemens Medical Solutions Diagnostics which include a license conferring rights in the human *in vitro* diagnostics field to the Applera patents for real-time PCR thermal cycling instruments and reagents. Under the agreements, Siemens will make up to a $24 million payment over 10 quarters, and potentially additional future royalties, to the Celera group for these rights.

- Also in September, the Celera group recorded a milestone payment from Merck & Co. Inc. in recognition of Merck s advancement of odanacatib (formerly MK-0822), an orally available highly selective inhibitor of the cathepsin K enzyme, into a Phase III clinical trial as a potential treatment for osteoporosis. If this candidate or others developed under the cathepsin K collaboration are advanced further toward commercialization, the Celera group will potentially receive additional milestone payments and royalties from Merck on net sales of products developed under the collaboration.

- In September, the Celera group and its collaborators published a paper in *Public Library of Science (Medicine)* describing novel variants in the *TRAF1/C5* gene region that predict individual susceptibility to, and severity of, rheumatoid arthritis ( RA ). Compared with non-carriers, carriers of the risk variants (about 65-70 percent of the general population) had an approximate 37 percent increased risk for developing RA.

- In September, the Celera group entered into a research collaboration with Merck & Co., Inc. to develop biomarker and pharmacogenomic tests for cancer patients. Under the terms of the agreement, the Celera group will evaluate the use of certain gene expression profiles identified by Merck with the goal of developing

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**APPLERA CORPORATION**

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

diagnostic predictors for use in Merck s clinical trials and to potentially form the basis for commercial companion diagnostic tests for oncology therapies.

- In September, the Celera group received notification from U.S. Food and Drug Administration that its Cystic Fibrosis Genotyping Assay had been cleared for marketing in the U.S.

We also note that in October 2007, the Celera group terminated its three year program for the development of an avian flu virus diagnostic test, which was supported in part by a grant from the National Institutes of Health. The termination was due primarily to a change in research and development focus because of the BHL acquisition. The Celera group has voluntarily relinquished the NIH grant funding for the final two years of the program.

**Critical Accounting Estimates**

There were no material changes to our critical accounting estimates during the first three months of fiscal 2008. For further information on our critical accounting estimates, refer to the discussion contained in the management s discussion and analysis section of our 2007 Annual Report to Stockholders (which discussion is incorporated in this quarterly report by reference).

**Events Impacting Comparability**

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

| Income/(charge) | Three months ended September 30, | |
|---|---|---|
| (Dollar amounts in millions) | **2007** | 2006 |
| Other charges | **$ -** | $ (3.5) |
| Total employee-related charges, asset impairments and other | **$ -** | $ (3.5) |
| Other events impacting comparability: | | |
| Asset dispositions and legal settlements | **$ 7.6** | $ (9.1) |
| Acquired research and development | | (114.3) |
| Tax items | **(1.8)** | 8.8 |

***Acquired Research and Development***

In the first quarter of fiscal 2007, the Applied Biosystems group recorded a $114.3 million charge to write-off the value of acquired in-process research and development ( IPR&D ) in connection with the acquisition of Agencourt Personal Genomics, Inc. ( APG ). As of the acquisition date, in July 2006, the technological feasibility of the acquired IPR&D project had not been established, and it was determined that the project had no future alternative use. The project being developed, which consists of both an instrument and reagents, is intended for very high throughput genetic analysis applications, including DNA sequencing and expression profiling.

At the date of acquisition, the project was in the development stage and approximately 30% complete. The work on the initial phase of this project was completed in September 2007. The following table briefly describes the APG project.

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APPLERA CORPORATION

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF

OPERATIONS continued

| | At Acquisition Date | | |
|---|---|---|---|
| | | Estimated | |
| (Dollar amounts in millions) | Fair Value | Costs to Complete | Approximate Percentage Completed |
| Instruments | **$ 66.6** | **$10.0** | **35%** |
| Reagents | **47.7** | **6.0** | **25%** |
| Total | **$ 114.3** | **$16.0** | |

In June 2007, we made our first placements of this next generation instrument system to early access customers. The initial instrument and reagents are expected to begin generating revenue in fiscal 2008. As of September 30, 2007, the total project costs were approximately $29 million, an increase of $13 million from the estimate as of the acquisition date. These additional R&D expenditures were for labor and materials required to accelerate the commercial launch of the platform and optimize features to better compete with other already commercialized next generation technologies. This increase in costs was offset by reductions in other planned R&D projects. Based on the performance of the system, the level of interest shown by our potential customers, and the progress in our manufacturing scale up, we accelerated the commercial release of the system to October 2007.

At the time of the acquisition, we believed there was a reasonable chance of realizing the economic return expected from the acquired in-process technology. We remain optimistic about the technology; however, as there is risk associated with the realization of benefits related to commercialization of an in-process project due to, among other things, rapidly changing customer needs, the complexity of the technology, growing competitive pressures, and potentially conflicting intellectual property rights of third parties, there can be no assurance that any project will meet commercial success.

***Employee-Related Charges, Asset Impairments and Other***

The following items have been recorded in the condensed consolidated statements of operations in employee-related charges, asset impairments and other, except as noted.

*Celera group*

Fiscal 2007

During the fourth quarter of fiscal 2007, the Celera group recorded a pre-tax charge of $0.5 million for severance costs for approximately 20 employees. The charge resulted from a reduction in the Celera group s proteomics-based activities. All of the affected employees were notified as of June 30, 2007, and were terminated by October 31, 2007. During the first quarter of fiscal 2008, we made cash payments of $0.4 million related to this charge. Cash expenditures were funded by available cash. The remaining cash expenditures of $0.1 million are expected to be paid in the second quarter of fiscal 2008. We believe this action will accelerate the Celera group s move to profitability, in part due to lower operating expenses.

During the first quarter of fiscal 2007, the Celera group recorded a pre-tax charge of $3.5 million for its estimated share of a damage award in continuing litigation between Abbott Laboratories, our alliance partner, and Innogenetics N.V. In September 2006, a jury found that the sale of hepatitis C virus ( HCV ) genotyping analyte specific reagents ( ASRs ) products by Abbott willfully infringed a U.S. patent owned by Innogenetics and awarded Innogenetics $7.0 million in damages. In January 2007, the U.S. District Court for the Western District of Wisconsin ruled in favor of Innogenetics request for a permanent injunction, and as such, ordered Abbott to withdraw its products from the market. The Court also reversed the jury verdict of willful infringement and ruled that Abbott did not willfully infringe Innogenetics patent and denied Innogenetics request for enhanced damages and attorneys fees. Innogenetics did not name the Celera group as a party in this lawsuit, but the Celera group has an interest in these products and in the outcome of the litigation because the enjoined products are manufactured by the Celera group and sold through its alliance with Abbott. Also, as these products are part of its alliance with Abbott, the Celera group has agreed to share the cost of this litigation, including the damage award described above. Abbott is appealing the judgment as both Abbott and the Celera group believe that Innogenetics patent is invalid and that the alliance s HCV genotyping ASRs do not infringe Innogenetics patent. On March 8, 2007, the Court of Appeals for the Federal Circuit issued an order denying Abbott s motion for a stay of the permanent injunction

APPLERA CORPORATION

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF

OPERATIONS continued

during the appeal process, and the alliance therefore will not receive any revenues from the sale of these HCV genotyping products for the foreseeable future. We believe the appeal process may take six months or more to conclude.

Charges prior to fiscal 2007

During fiscal 2006, the Celera group recorded pre-tax charges of $26.4 million related to its decision to exit its small molecule drug discovery and development programs and the integration of Celera Diagnostics into the Celera group. These charges consisted of $12.8 million of employee-related charges, $9.8 million of asset impairments, $1.2 million of excess lease space, and $2.6 million of other disposal costs. The remaining required cash expenditures of $0.9 million as of September 30, 2007, the majority of which related to the asset impairment of an owned facility, are expected to be disbursed by December 31, 2007.

During the first three months of fiscal 2008, the Celera group made net cash payments of approximately $0.2 million related to an excess facility lease space charge for our discontinued Paracel business that was recorded in fiscal 2005. The remaining net cash expenditures of approximately $2.5 million as of September 30, 2007 related to this charge are expected to be disbursed by fiscal 2011.

*Applied Biosystems group*

Charges prior to fiscal 2007

During the first three months of fiscal 2008, the Applied Biosystems group made cash payments of approximately $0.4 million related to excess facility lease space charges recorded in fiscal 2005. The remaining cash payments of $0.2 million as of September 30, 2007 are expected to be disbursed by fiscal 2011.

***Other Events Impacting Comparability***

*Asset dispositions and legal settlements*

The following items have been recorded in the condensed consolidated statements of operations in asset dispositions and legal settlements.

Fiscal 2008

In the first quarter of fiscal 2008, the Applied Biosystems group recorded a $7.6 million pre-tax gain primarily related to a settlement and licensing agreement entered into with Stratagene Corporation and Agilent Technologies, Inc. (which acquired Stratagene), which resolved outstanding legal disputes with Stratagene.

Fiscal 2007

In the first quarter of fiscal 2007, the Applied Biosystems group recorded a $9.1 million pre-tax charge related to a settlement agreement entered into with another company which resolved outstanding legal disputes with that company.

*Tax items*

Fiscal 2008

In the first quarter of fiscal 2008, the Applied Biosystems group recorded tax charges of $1.8 million primarily related to the recalculation of deferred tax assets as a result of a decrease in the statutory tax rate in Germany.

Fiscal 2007

In the first quarter of fiscal 2007, the Applied Biosystems group recorded a tax benefit of $8.8 million related to a reduction in the valuation allowance for German net operating loss carryforwards.

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APPLERA CORPORATION

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

**Discussion of Applera Corporation s Consolidated Operations**

| (Dollar amounts in millions) | Three Months Ended September 30, 2007 | 2006 | % Increase/ (Decrease) |
|---|---|---|---|
| Net revenues | **$516.7** | $485.4 | **6.4%** |
| Cost of sales | **224.3** | 224.1 | **0.1%** |
| Gross margin | **292.4** | 261.3 | **11.9%** |
| SG&A expenses | **156.5** | 142.3 | **10.0%** |
| R&D | **60.8** | 57.9 | **5.0%** |
| Amortization of purchased intangible assets | **2.6** | 2.7 | **(3.7%)** |
| Employee-related charges, asset impairments and other | | 3.5 | **(100.0%)** |
| Asset dispositions and legal settlements | **(7.6)** | 9.1 | **(183.5%)** |
| Acquired research and development | | 114.3 | **(100.0%)** |
| Operating income (loss) | **80.1** | (68.5) | **(216.9%)** |
| Gain on investments, net | | 0.2 | **(100.0%)** |
| Interest income, net | **10.8** | 9.2 | **17.4%** |
| Other income (expense), net | **0.8** | 1.4 | **(42.9%)** |
| Income (loss) before income taxes | **91.7** | (57.7) | **(258.9%)** |
| Provision for income taxes | **30.0** | 8.3 | **261.4%** |
| Net income (loss) | **$ 61.7** | $(66.0) | **(193.5%)** |
| Percentage of net revenues: | | | |
| Gross margin | **56.6%** | 53.8% | |
| SG&A expenses | **30.3%** | 29.3% | |
| R&D | **11.8%** | 11.9% | |
| Operating income (loss) | **15.5%** | (14.1%) | |
| Effective income tax rate | **32.7%** | 14.4% | |

The following table summarizes the impact of the previously described events impacting comparability included in the financial results for fiscal 2008 and 2007:

| (Dollar amounts in millions) | Three Months Ended September 30, 2007 | 2006 |
|---|---|---|
| Income (charge) included in income (loss) before income taxes | **$7.6** | $(126.9) |
| Charge (benefit) for income taxes | **4.0** | (12.7) |

We reported net income in the first quarter of fiscal 2008 compared to a net loss in the first quarter of fiscal 2007. This change primarily resulted from the previously described events impacting comparability, in particular the acquired research and development charge recorded in fiscal 2007, and higher net revenues, partially offset by higher operating expenses. The net effect of foreign currency on our net income was a benefit of approximately $6 million during the first quarter of fiscal 2008 as compared to the prior year quarter. Read our discussion of segments for information on their financial results.

Net revenues, which include the favorable effects of foreign currency, increased in the first quarter of fiscal 2008 compared with the prior year quarter. The effect of foreign currency increased net revenues by approximately 2% for the first quarter of fiscal 2008 as compared to the prior year quarter.

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**APPLERA CORPORATION**

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

- Net revenues increased for the quarter at the Applied Biosystems group, driven by strength in the Real-Time PCR/Applied Genomics product category, primarily due to higher sales of consumables products, and in the Mass Spectrometry category, primarily due to higher instrument service contract revenues. Lower instrument sales in the DNA Sequencing product category were partially offset by higher consumables sales in that category.
- Net revenues increased at the Celera group, primarily due to $5.0 million of net revenues related to the achievement of a drug development license milestone by a third party and the resale of a small molecule drug development program and $2.4 million from the licensing of real-time PCR thermal cycling instruments and reagents. Also contributing to the increase in reported revenues were higher royalties from other diagnostic licensees. The increase in reported revenues was partially offset by a lower equalization payment from Abbott compared to the prior year quarter.

In Europe, revenues increased approximately 11% during the first quarter of fiscal 2008 as compared to the prior year quarter, which included the favorable effect of foreign currency of approximately 6%. Excluding the effects of foreign currency, revenues increased by approximately 5% in Europe, primarily as a result of sales of DNA sequencing consumables, TaqMan® Gene Expression Assay products, Q TRAP® systems, and API triple quadrupole, or quad, systems. This growth was partially offset by lower sales of low to medium throughput genetic analyzers and MALDI TOF/TOF systems. Sales in the U.S. increased primarily due to sales of API triple quad systems, TaqMan Gene Expression Assay products, Real-Time PCR consumables, and human identification consumables. This increase was partially offset by lower sales of genetic analyzers and low throughput Real-Time PCR instruments in fiscal 2008 and the inclusion of a U.S. Department of Defense contract for an instrument system recorded in the first quarter of fiscal 2007. Revenues in Asia Pacific, other than Japan, increased by approximately 8% as compared to the prior year quarter, including a favorable impact from foreign currency of approximately 2%. This growth was led by Australia and China. From a product perspective in Asia Pacific, other than Japan, revenue increased due to higher sales of high throughput genetic analyzers, human identification consumables, and Q TRAP systems, partially offset by lower sales of API triple quad systems. Revenues in Japan during the first quarter of fiscal 2008 increased by approximately 2% relative to the prior year quarter. This increase was primarily driven by a favorable impact from foreign currency of approximately 3%, which was partially offset by lower sales of API triple quad systems in the region. The Asia Pacific category includes revenues from India and other countries in West Asia, which had previously been managed by our Europe region. Revenues by geographic area for the first quarter of fiscal 2007 have been reclassified to reflect this change.

The higher gross margin percentage for the first quarter of fiscal 2008 as compared to the prior year quarter was primarily due to: lower costs for enzymes due to a combination of improved vendor pricing and lower manufacturing costs, the favorable effects of foreign currency, and higher royalty and license revenue, all at the Applied Biosystems group, and higher licensing and collaboration revenues at the Celera group, partially offset by inventory-related costs for the 1700 reader for our Gene Expression Arrays, a discontinued product line at the Applied Biosystems group, and the inclusion in the first quarter of fiscal 2007 of a U.S. Department of Defense contract awarded to the Applied Biosystems group in August 2006.

SG&A expenses for the first quarter of fiscal 2008 increased compared to the prior year quarter primarily due to: the reversal in the first quarter of fiscal 2007 of a $5 million accrual related to settled litigation; regional investments, including additional headcount, of approximately $5 million in fiscal 2008 to support growth primarily in Europe and China; higher employee-related costs, net of sales commissions, of approximately $3 million; and the unfavorable impact of foreign currency of approximately $3 million, all at the Applied Biosystems group. The first quarter of fiscal 2008 for both the Applied Biosystems group and the Celera group included expenses related to the review of our corporate structure.

R&D expenses increased for the first quarter of fiscal 2008 compared to the prior year quarter primarily as a result of investments in the SOLiD program, the next-generation DNA sequencing system, and higher employee-related costs at the Applied Biosystems group, partially offset by reduced proteomics discovery spending at the Celera group.

Interest income, net increased during the first quarter of fiscal 2008 compared to the same quarter last year primarily due to higher average cash and cash equivalents and short-term investments and higher average interest rates, partially offset by interest expense incurred on our loans payable.

**APPLERA CORPORATION**

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

The year over year change in the effective tax rate was primarily due to the previously described events impacting comparability; in particular, the tax item recorded in the first quarter of fiscal 2007 and the charge recorded for acquired IPR&D in the first quarter of fiscal 2007 which did not generate a tax benefit.

**Applera Corporation**

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

We had cash and cash equivalents and short-term investments of $825.3 million at September 30, 2007, and $1,056.0 million at June 30, 2007. We maintain a $250 million unsecured revolving credit agreement with four banks that matures on May 25, 2012. This amount was increased from $200 million effective August 27, 2007, at our request in accordance with the terms of the agreement. There was $175 million outstanding under this agreement at September 30, 2007. On August 27, 2007, we entered into a $100 million unsecured term loan agreement with Bank of America, N.A. that matures on September 4, 2008. Upon the satisfaction of various conditions, we have the option to extend the maturity date on this agreement to September 4, 2010. There was $100 million outstanding under this agreement at September 30, 2007. Both the revolving credit agreement and the term loan agreement require that we maintain a debt to total capital ratio, as defined in each agreement, of not more than 0.50:1:00. See Note 8 to our condensed consolidated financial statements for more information on our loans payable. The amounts borrowed under these agreements were used to fund the repurchase of shares of Applera-Applied Biosystems group stock and were allocated entirely to the Applied Biosystems group. Cash provided by operating activities and our debt borrowings have been our primary source of funds over the last fiscal year.

In April 2007, we announced that our board of directors authorized the repurchase of up to 10% of the outstanding shares of Applera-Applied Biosystems stock. This authorization has no time restrictions and delegates to management discretion to purchase shares at times and prices it deems appropriate through open market purchases, privately negotiated transactions, tender offers, exchange offers, or otherwise. We repurchased 3.4 million shares of Applera-Applied Biosystems stock for approximately $100 million during the fourth quarter of fiscal 2007 under this authorization. Subsequently, on August 8, 2007, we announced that our board of directors increased this authorization to $1.2 billion, which at market prices on that date represented approximately 20% of the outstanding shares of Applera-Applied Biosystems stock. Pursuant to this authorization, we entered into an agreement with Morgan Stanley in August 2007 for the accelerated repurchase of $600 million of Applera-Applied Biosystems stock. During the first quarter of fiscal 2008, we paid Morgan Stanley approximately $602 million for this transaction, of which $327 million was funded by cash and $275 million was funded by bank loans. These authorizations supplement the board s standing authorization to replenish shares of Applera-Applied Biosystems stock issued under our employee stock benefit plans.

We believe that existing funds, cash generated from operations, and existing sources of debt financing are more than adequate to satisfy our normal operating cash flow needs, planned capital expenditures, acquisitions, authorized share repurchases, and dividends for the next twelve months and for the foreseeable future.

| (Dollar amounts in millions) | **September 30, 2007** | June 30, 2007 |
|---|---|---|
| Cash and cash equivalents | **$464.4** | $ 323.2 |
| Short-term investments | **360.9** | 732.8 |
| Total cash and cash equivalents and short-term investments | **$825.3** | $1,056.0 |
| Total debt | **275.0** | |
| Working capital | **783.2** | 1,215.4 |
| Debt to total capitalization | **13.0%** | |

Cash and cash equivalents increased for the first three months of fiscal 2008 from June 30, 2007, as cash generated from operating activities, proceeds from bank loans, sales of investments, net of purchases, and stock issuances exceeded the payment to Morgan Stanley for the accelerated share repurchase transaction, cash expenditures for the purchase of capital and other assets, net of sales, and the payment of dividends.

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**APPLERA CORPORATION**

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

Net cash flows of continuing operations for the first quarter ended September 30 were as follows:

| (Dollar amounts in millions) | **2007** | 2006 |
|---|---|---|
| Net cash from operating activities | **$ 82.7** | $ 8.7 |
| Net cash from investing activities | **361.9** | (191.9) |
| Net cash from financing activities | **(313.6)** | 26.7 |
| Effect of exchange rate changes on cash | **(2.7)** | 5.3 |

*Operating activities:*

The increase in net cash provided from operating activities for the first three months of fiscal 2008 compared to the first three months of fiscal 2007 resulted primarily from higher income-related cash flows, a lower use of cash in accounts payable and other liabilities, and a higher source of cash in prepaid expenses and other assets, partially offset by a higher use of cash in accounts receivable. The lower use of cash in accounts payable and other liabilities resulted primarily from the timing of vendor and royalty payments and tax refunds received in the first quarter of fiscal 2008 primarily due to the completion of foreign tax audits. The higher source of cash in prepaid expenses and other assets resulted primarily from the timing of receipts of dividends and distributions related to the Applied Biosystems group s joint venture activities. The higher use of cash in accounts receivable was due in part to the timing of the collection of licensing and milestone payments recorded in the first quarter of fiscal 2008 at the Celera group, as well as the equalization payment from Abbott received at the beginning of the second quarter of fiscal 2008. The Applied Biosystems group s days sales outstanding was 64 days at September 30, 2007, compared to 58 days at June 30, 2007 and 55 days at September 30, 2006. The increase resulted primarily from lower collections, primarily outside of North America, and increased royalty receivables. Inventory on hand was 3.6 months at September 30, 2007, compared to 2.7 months at June 30, 2007. The increase was primarily related to the SOLiD program and the timing of manufacturing work in progress and inventory receipts.

*Investing activities:*

Capital expenditures, net of disposals, for the first quarter of fiscal 2008 were $5.2 million lower than in the prior year quarter primarily due to expenditures for the Applied Biosystems Portal in the first quarter of fiscal 2007. The first three months of fiscal 2008 included higher proceeds, net of purchases, from sales and maturities of available for sale investments. In July 2006, we acquired APG for approximately $121 million, including transaction costs.

*Financing activities:*

During the first three months of fiscal 2008, we paid Morgan Stanley approximately $602 million for the accelerated share repurchase transaction, of which $275 million was funded by bank loans and the balance with cash. During the first quarter of fiscal 2008, we borrowed $175 million under our $250 million unsecured revolving credit agreement and $100 million under our unsecured term loan agreement. See Note 8 to our condensed consolidated financial statements for more information on our loans payable.

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**APPLERA CORPORATION**

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

**Contractual Obligations**

Our significant contractual obligations at September 30, 2007, and the anticipated payments under these obligations were as follows:

| | | Payments by Period | | | |
|---|---|---|---|---|---|
| (Dollar amounts in millions) | Total | 2008 [a] | 2009 - 2010 | 2011 - 2012 | Thereafter |
| Minimum operating lease payments [b] | **$135.0** | **$ 30.3** | **$56.9** | **$23.2** | **$24.6** |
| Purchase obligations [c] | **164.6** | **120.4** | **31.7** | **9.4** | **3.1** |
| Other long-term liabilities [d] | **40.9** | **2.8** | **2.2** | **1.6** | **34.3** |
| Total | **$340.5** | **$153.5** | **$90.8** | **$34.2** | **$62.0** |

We adopted Financial Accounting Standards Board ( FASB ) Interpretation No. ( FIN ) 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 on July 1, 2007. The amount of unrecognized tax benefits at July 1, 2007 was $67.9 million. This amount has been excluded from the contractual obligations table because we are unable to reasonably predict the ultimate amount or timing of future tax settlements.

[a] Represents cash obligations for the remainder of fiscal 2008.
[b] Refer to Note 10 to our consolidated financial statements in our 2007 Annual Report to Stockholders for further information.
[c] Purchase obligations are entered into with various vendors in the normal course of business, and include commitments related to inventory, capital expenditures, R&D arrangements and collaborations, license agreements, and other services.
[d] We have excluded deferred revenues as they have no impact on our future liquidity. We have also excluded deferred tax liabilities and obligations connected with our pension and postretirement plans and other foreign employee-related plans as they are not contractually fixed as to timing and amount. See Note 11 to our condensed consolidated financial statements contained in this report and Note 5 to our consolidated financial statements in our 2007 Annual Report to Stockholders for more information on these plans.

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**APPLERA CORPORATION**

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

**Discussion of Segments Operations, Financial Resources and Liquidity**

***Applied Biosystems Group***

| | Three Months Ended September 30, | | % Increase/ |
|---|---|---|---|
| (Dollar amounts in millions) | **2007** | 2006 | **(Decrease)** |
| Net revenues | **$501.2** | $476.3 | **5.2%** |
| Cost of sales | **221.3** | 220.7 | **0.3%** |
| Gross margin | **279.9** | 255.6 | **9.5%** |
| SG&A expenses | **148.4** | 135.1 | **9.8%** |
| R&D | **50.6** | 45.1 | **12.2%** |
| Amortization of purchased intangible assets | **2.6** | 2.7 | **(3.7%)** |
| Asset dispositions and legal settlements | **(7.6)** | 9.1 | **(183.5%)** |
| Acquired research and development | | 114.3 | **(100.0%)** |
| Operating income (loss) | **85.9** | (50.7) | **(269.4%)** |
| Gain on investments, net | | 0.2 | **(100.0%)** |
| Interest income, net | **3.6** | 2.6 | **38.5%** |
| Other income (expense), net | **1.1** | 1.3 | **(15.4%)** |
| Income (loss) before income taxes | **90.6** | (46.6) | **(294.4%)** |
| Provision for income taxes | **29.7** | 12.1 | **145.5%** |
| Net income (loss) | **$ 60.9** | $ (58.7) | **(203.7%)** |
| Percentage of net revenues: | | | |
| Gross margin | **55.8%** | 53.7% | |
| SG&A expenses | **29.6%** | 28.4% | |
| R&D | **10.1%** | 9.5% | |
| Operating income (loss) | **17.1%** | (10.6%) | |
| Effective income tax rate | **32.8%** | 26.0% | |

The following table summarizes the impact of the previously described events impacting comparability included in the financial results for fiscal 2008 and 2007:

| | Three Months Ended September 30, | |
|---|---|---|
| (Dollar amounts in millions) | **2007** | 2006 |
| Income (charge) included in income (loss) before income taxes | **$7.6** | $(123.4) |
| Charge (benefit) for income taxes | **4.2** | (11.7) |

The Applied Biosystems group reported net income in the first quarter of fiscal 2008 compared to a net loss in the first quarter of fiscal 2007. This change primarily resulted from the previously described events impacting comparability, in particular the acquired research and development charge recorded in fiscal 2007, and higher net revenues, partially offset by higher operating expenses. The net effect of foreign currency on our net income was a benefit of approximately $6 million during the first quarter of fiscal 2008 as compared to the prior year quarter.

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**APPLERA CORPORATION**

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

*Revenues overall summary*

The following table sets forth the Applied Biosystems group s revenues by product categories for the three months ended September 30:

| | Three Months Ended September 30, | | % Increase/ |
|---|---|---|---|
| (Dollar amounts in millions) | **2007** | 2006 | **(Decrease)** |
| DNA Sequencing | **$ 129.0** | $ 131.5 | **(2%)** |
| *% of total revenues* | ***26%*** | *28%* | |
| Real-Time PCR/Applied Genomics | **180.1** | 156.1 | **15%** |
| *% of total revenues* | ***36%*** | *33%* | |
| Mass Spectrometry | **121.1** | 116.0 | **4%** |
| *% of total revenues* | ***24%*** | *24%* | |
| Core PCR & DNA Synthesis | **46.6** | 46.2 | **1%** |
| *% of total revenues* | ***9%*** | *10%* | |
| Other Product Lines | **24.4** | 26.5 | **(8%)** |
| *% of total revenues* | ***5%*** | *5%* | |
| Total | **$ 501.2** | $ 476.3 | **5%** |

The effect of foreign currency increased net revenues in the first quarter of fiscal 2008 by approximately 2% as compared to the prior year quarter.

Real-Time PCR/Applied Genomics:

- Revenues in the Real-Time PCR/Applied Genomics product category increased primarily due to higher sales of consumable products, including human identification kits used in forensics, TaqMan Gene Expression Assay products, sequence detection consumables, and consumables related to our Ambion business that we acquired in fiscal 2006. This category is increasingly driven by application-specific reagent products.