10-Q 1 secondqtrtenq.txt UNITED STATES SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549 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 July 3, 2005 or ( ) Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the for the transition period from to Commission file number 1-3215 JOHNSON & JOHNSON (Exact name of registrant as specified in its charter) NEW JERSEY 22-1024240 (State or other jurisdiction of (I.R.S. Employer Incorporation or organization) Identification No.) One Johnson & Johnson Plaza New Brunswick, New Jersey 08933 (Address of principal executive offices) Registrant's telephone number, including area code (732) 524-0400 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 an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes (X) No ( ) Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. On July 31, 2005, 2,974,694,094 shares of Common Stock, $1.00 par value, were outstanding. 1 JOHNSON & JOHNSON AND SUBSIDIARIES TABLE OF CONTENTS Part I - Financial Information Page No. Item 1. Financial Statements (unaudited) Consolidated Balance Sheets - July 3, 2005 and January 2, 2005 3 Consolidated Statements of Earnings for the Fiscal Quarters Ended July 3, 2005 and June 27, 2004 6 Consolidated Statements of Earnings for the Fiscal Six Months Ended July 3, 2005 and June 27, 2004 7 Consolidated Statements of Cash Flows for the Fiscal Six Months Ended July 3, 2005 and June 27, 2004 8 Notes to Consolidated Financial Statements 10 Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations 30 Item 3. Quantitative and Qualitative Disclosures About Market Risk 40 Item 4. Controls and Procedures 40 Part II - Other Information Item 1 - Legal Proceedings 41 Item 2 - Unregistered Sales of Equity Securities and Use of Proceeds 41 Item 4 - Submission of Matters to a Vote of Security Holders 41 Item 6 - Exhibits 42 Signatures 43 2 Part I - FINANCIAL INFORMATION Item 1 - Financial Statements JOHNSON & JOHNSON AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS (Unaudited; Dollars in Millions) ASSETS July 3, January 2, 2005 2005 Current Assets: Cash and cash equivalents $12,156 9,203 Marketable securities 1,005 3,681 Accounts receivable, trade, less allowances for doubtful accounts $180(2004, $206) 7,379 6,831 Inventories (Note 4) 3,963 3,744 Deferred taxes on income 1,830 1,737 Prepaid expenses and other current assets 2,387 2,124 Total current assets 28,720 27,320 Marketable securities, non-current 49 46 Property, plant and equipment, at cost 18,672 18,664 Less accumulated depreciation 8,581 8,228 Property, plant and equipment, net 10,091 10,436 Intangible assets (Note 5) 15,681 15,105 Less accumulated amortization 3,486 3,263 Intangible assets, net 12,195 11,842 Deferred taxes on income 363 551 Other assets 3,135 3,122 Total assets $54,553 53,317 See Notes to Consolidated Financial Statements 3 JOHNSON & JOHNSON AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS (Unaudited; Dollars in Millions) LIABILITIES AND SHAREHOLDERS' EQUITY July 3, January 2, 2005 2005 Current Liabilities: Loans and notes payable $ 304 280 Accounts payable 3,949 5,227 Accrued liabilities 3,153 3,523 Accrued rebates, returns and promotions 2,312 2,297 Accrued salaries, wages and commissions 892 1,094 Taxes on income 1,030 1,506 Total current liabilities 11,640 13,927 Long-term debt 2,329 2,565 Deferred tax liability 418 403 Employee related obligations 2,936 2,631 Other liabilities 2,061 1,978 Total liabilities 19,384 21,504 Shareholders' equity: Preferred stock - without par value (authorized and unissued 2,000,000 shares) - - Common stock - par value $1.00 per share (authorized 4,320,000,000 shares; issued 3,119,842,000 shares) 3,120 3,120 Note receivable from employee stock ownership plan - (11) Accumulated other comprehensive income (Note 8) (805) (515) Retained earnings 38,853 35,223 4 Less common stock held in treasury, at cost (145,646,000 & 148,819,000 shares) 5,999 6,004 Total shareholders' equity 35,169 31,813 Total liabilities and shareholders' equity $54,553 53,317 See Notes to Consolidated Financial Statements 5 JOHNSON & JOHNSON AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF EARNINGS (Unaudited; dollars & shares in millions except per share figures) Fiscal Second Quarter Ended July 3, Percent June 27, Percent 2005 to Sales 2004 to Sales Sales to customers (Note 6) $12,762 100.0% 11,484 100.0 Cost of products sold 3,508 27.5 3,162 27.5 Gross profit 9,254 72.5 8,322 72.5 Selling, marketing and administrative expenses 4,194 32.8 3,711 32.3 Research expense 1,487 11.6 1,182 10.3 Purchased in-process research and development 353 2.8 - - Interest income (109) (.8) (35) (.3) Interest expense, net of portion capitalized 15 .1 52 .4 Other (income)expense, net (88) (.7) (23) (.1) Earnings before provision for taxes on income 3,402 26.7 3,435 29.9 Provision for taxes on income (Note 3) 726 5.7 977 8.5 NET EARNINGS $2,676 21.0 2,458 21.4 NET EARNINGS PER SHARE (Note 7) Basic $ .90 .83 Diluted $ .89 .82 CASH DIVIDENDS PER SHARE $ .33 .285 AVG. SHARES OUTSTANDING Basic 2,973.7 2,968.2 Diluted 3,024.7 3,005.3 See Notes to Consolidated Financial Statements 6 JOHNSON & JOHNSON AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF EARNINGS (Unaudited; dollars & shares in millions except per share figures) Fiscal Six Months Ended July 3, Percent June 27, Percent 2005 to Sales 2004 to Sales Sales to customers (Note 6) $25,594 100.0% 23,043 100.0 Cost of products sold 6,990 27.3 6,529 28.3 Gross profit 18,604 72.7 16,514 71.7 Selling, marketing and administrative expenses 8,237 32.1 7,351 31.9 Research expense 2,834 11.1 2,278 9.9 Purchased in-process research and development 353 1.4 - - Interest income (193) (0.7) (74) (.3) Interest expense, net of portion capitalized 30 0.1 97 .4 Other (income)expense, net (121) (.5) (77) (.3) Earnings before provision for taxes on income 7,464 29.2 6,939 30.1 Provision for taxes on income (Note 3) 1,861 7.3 1,988 8.6 NET EARNINGS $5,603 21.9 4,951 21.5 NET EARNINGS PER SHARE (Note 7) Basic $ 1.88 1.67 Diluted $ 1.86 1.65 CASH DIVIDENDS PER SHARE $ .615 .525 AVG. SHARES OUTSTANDING Basic 2,973.0 2,968.1 Diluted 3,021.8 3,004.4 See Notes to Consolidated Financial Statements 7 JOHNSON & JOHNSON AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited; Dollars in Millions) Fiscal Six Months Ended July 3, June 27, 2005 2004 CASH FLOWS FROM OPERATIONS Net earnings $ 5,603 4,951 Adjustment to reconcile net earnings to cash flows: Depreciation and amortization of property and intangibles 1,063 1,027 Purchased in-process research and development 353 - Deferred tax provision (117) (429) Accounts receivable allowances (17) 2 Changes in assets and liabilities, net of effects from acquisition of businesses: Increase in accounts receivable (876) (624) (Increase) decrease in inventories (380) 23 Decrease in accounts payable and accrued liabilities (1,651) (1,146) Decrease in other current and non-current assets 578 248 Increase in other current and non-current liabilities 131 729 NET CASH FLOWS FROM OPERATING ACTIVITIES 4,687 4,781 CASH FLOWS FROM INVESTING ACTIVITIES Additions to property, plant and equipment (874) (714) Proceeds from the disposal of assets 77 233 Acquisitions, net of cash acquired (693) (300) Purchases of investments (4,999) (5,654) Sales of investments 7,611 4,684 Other (282) (113) NET CASH PROVIDED/(USED) BY INVESTING ACTIVITIES 840 (1,864) CASH FLOWS FROM FINANCING ACTIVITIES Dividends to shareholders (1,829) (1,559) Repurchase of common stock (988) (760) Proceeds from short-term debt 351 332 Retirement of short-term debt (314) (911) Proceeds from long-term debt 4 16 Retirement of long-term debt (20) (1) Proceeds from the exercise of stock options 417 311 8 NET CASH USED BY FINANCING ACTIVITIES (2,379) (2,572) Effect of

exchange rate changes on cash and cash equivalents (195) (41) Increase in cash and cash equivalents 2,953 304 Cash and cash equivalents, beginning of period 9,203 5,377 CASH AND CASH EQUIVALENTS, END OF PERIOD $12,156 5,681 ACQUISITIONS Fair value of assets acquired 854 339 Fair value of liabilities assumed (161) (39) Net cash paid for acquisitions $ 693 300 See Notes to Consolidated Financial Statements 9 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS NOTE 1 - The accompanying unaudited interim financial statements and related notes should be read in conjunction with the Consolidated Financial Statements of Johnson & Johnson and Subsidiaries (the "Company") and related notes as contained in the Company's Annual Report on Form 10-K for the fiscal year ended January 2, 2005. The unaudited interim financial statements include all adjustments (consisting only of normal recurring adjustments) and accruals necessary in the judgment of management for a fair statement of the results for the periods presented. NOTE 2 - FINANCIAL INSTRUMENTS The Company follows the provisions of Statement of Financial Accounting Standards (SFAS) 133, SFAS 138 and SFAS 149 requiring that all derivative instruments be recorded on the balance sheet at fair value. As of July 3, 2005, the balance of deferred net losses on derivatives included in accumulated other comprehensive income was $65 million after-tax. The Company expects that substantially all of this amount will be reclassified into earnings over the next 12 months as a result of transactions that are expected to occur over that period. The amount ultimately realized in earnings will differ as foreign exchange rates change. Realized gains and losses are ultimately determined by actual exchange rates at maturity of the derivative. Transactions with third parties will cause the amount in accumulated other comprehensive income to affect net earnings. The maximum length of time over which the Company is hedging is 18 months. The Company also uses currency swaps to manage currency risk primarily related to borrowings, which may exceed 18 months. For the first fiscal six months ended July 3, 2005, the net impact of the hedges' ineffectiveness to the Company's financial statements was insignificant. For the first fiscal six months ended July 3, 2005, the Company has recorded a net loss of $3 million after tax in other (income) expense, representing the impact of discontinuance of cash flow hedges because it is probable that the originally forecasted transactions will not occur by the end of the originally specified time period. Refer to Note 8 for disclosures of movements in Accumulated Other Comprehensive Income. NOTE 3 - INCOME TAXES The worldwide effective income tax rates for the first fiscal six months of 2005 and 2004 were 24.9% and 28.6%, a decrease of 3.7%. Of this decrease, 1.9% was attributed to increases in taxable income in lower tax jurisdictions relative to taxable income in higher tax jurisdictions. The remaining net decrease of 1.8% was attributed to a one-time tax benefit partially offset by IPR&D, as described below. Acquisition related In-process Research & Development (IPR&D) charges of $353 million that are non- deductible for tax purposes were recorded in the fiscal second quarter of 2005. 10 The fiscal second quarter of 2005 included a benefit of $225 million, due to the reversal of a tax liability previously recorded during the fiscal fourth quarter of 2004, associated with a technical correction made to the American Jobs Creation Act of 2004, in May 2005. NOTE 4 - INVENTORIES (Dollars in Millions) July 3, 2005 January 2, 2005 Raw materials and supplies $ 1,193 964 Goods in process 1,134 1,113 Finished goods 1,636 1,667 $ 3,963 3,744 NOTE 5 - INTANGIBLE ASSETS Intangible assets that have finite useful lives are amortized over their estimated useful lives. Goodwill and indefinite lived intangible assets are assessed annually for impairment. The latest impairment assessment of goodwill and indefinite lived intangible assets was completed in the fiscal fourth quarter of 2004 and no impairment was determined. Future impairment tests will be performed annually in the fiscal fourth quarter, or sooner if warranted by economic conditions. (Dollars in Millions) July 3, 2005 January 2, 2005 Goodwill $ 6,716 6,597 Less accumulated amortization 714 734 Goodwill - net 6,002 5,863 Trademarks (non-amortizable) 1,205 1,232 Less accumulated amortization 139 142 Trademarks (non- amortizable)- net 1,066 1,090 Patents and trademarks 4,175 3,974 Less accumulated amortization 1,272 1,125 Patents and trademarks - net 2,903 2,849 Other amortizable intangibles 3,585 3,302 Less accumulated amortization 1,361 1,262 Other intangibles - net 2,224 2,040 Total intangible assets 15,681 15,105 Less accumulated amortization 3,486 3,263 Total intangibles - net $12,195 11,842 11 Goodwill as of July 3, 2005 as allocated by segment of business is as follows: (Dollars in Millions) Med. Dev Consumer Pharm & Diag Total Goodwill, net at January 2, 2005 $1,160 832 3,871 5,863 Acquisitions - 71 184 255 Translation (62) (25) (29) (116) Goodwill, net as of July 3, 2005 $1,098 878 4,026 6,002 The weighted average amortization periods for patents and trademarks and other intangible assets are 15 years and 17 years, respectively. The amortization expense of amortizable intangible assets for the fiscal six months ended July 3, 2005 was $262 million and the estimated amortization expense for the five succeeding years approximates $550 million, annually. NOTE 6 - SEGMENTS OF BUSINESS AND GEOGRAPHIC AREAS (Dollars in Millions) SALES BY SEGMENT OF BUSINESS (1) Fiscal Second Quarter Percent 2005 2004 Change Consumer U.S. $ 1,092 987 10.6% International 1,186 1,013 17.1 2,278 2,000 13.9 Pharmaceutical U.S. $ 3,595 3,643 (1.3)% International 2,033 1,784 14.0 5,628 5,427 3.7 Med Devices and Diagnostics U.S. $ 2,378 2,038 16.7% International 2,478 2,019 22.7 4,856 4,057 19.7 U.S. $ 7,065 6,668 6.0% International 5,697 4,816 18.3 Worldwide $ 12,762 11,484 11.1% 12 Fiscal Six Months Percent 2005 2004 Change Consumer U.S. $ 2,206 2,067 6.7% International 2,352 1,980 18.8 4,558 4,047 12.6 Pharmaceutical U.S. $ 7,378 7,286 1.3% International 4,005 3,517 13.9 11,383 10,803 5.4 Med Devices and Diagnostics U.S. $ 4,739 4,233 12.0% International 4,914 3,960 24.1 9,653 8,193 17.8 U.S. $ 14,323 13,586 5.4% International 11,271 9,457 19.2 Worldwide $ 25,594 23,043 11.1% (1) Export and intersegment sales are not significant. OPERATING PROFIT BY SEGMENT OF BUSINESS Fiscal Second Quarter Percent 2005 2004 Change Consumer $ 418 382 9.4% Pharmaceutical(1) 1,585 2,108 (24.8) Med. Dev. & Diag.(2) 1,409 1,055 33.6 Segments total 3,412 3,545 (3.8) Expenses not allocated to segments (10) (110) Worldwide total $ 3,402 3,435 (1.0)% Fiscal Six Months Percent 2005 2004 Change Consumer $ 875 829 5.5% Pharmaceutical(1) 3,722 4,194 (11.3) Med. Dev. & Diag. (2) 2,902 2,118 37.0 Segments total 7,499 7,141 5.0 Expenses not allocated to segments (35) (202) Worldwide total $ 7,464 6,939 7.6% (1) Includes $302 million of IPR&D charges related to acquisitions 13 completed in the fiscal second quarter of 2005. (2) Includes $51 million of IPR&D charges related to acquisitions completed in the fiscal second quarter of 2005. SALES BY GEOGRAPHIC AREA Fiscal Second Quarter Percent 2005 2004 Change U.S. $ 7,065 6,668 6.0% Europe 3,186 2,779 14.6 Western Hemisphere, excluding U.S. 751 622 20.7 Asia-Pacific, Africa 1,760 1,415 24.4 Total $ 12,762 11,484 11.1% Fiscal Six Months Percent 2005 2004 Change U.S. $ 14,323 13,586 5.4% Europe 6,362 5,486 16.0 Western Hemisphere, excluding U.S. 1,477 1,219 21.2 Asia-Pacific, Africa 3,432 2,752 24.7 Total $ 25,594 23,043 11.1% NOTE 7 - EARNINGS PER SHARE The following is a reconciliation of basic net earnings per share to diluted net earnings per share for the fiscal second quarters ended July 3, 2005 and June 27, 2004. (Shares in Millions) Fiscal Second Quarter Ended July 3, June 27, 2005 2004 Basic net earnings per share $ .90 .83 Average shares outstanding - basic 2,973.7 2,968.2 Potential shares exercisable under stock option plans 260.2 152.8 Less: shares which could be repurchased under treasury stock method (216.6) (130.5) Convertible debt shares 7.4 14.8 Average shares outstanding - diluted 3,024.7 3,005.3 Diluted earnings per share $ .89 .82 14 The diluted earnings per share calculation included the dilutive effect of convertible debt that was offset by the related reduction in interest expense of $3 million each for the fiscal second quarters ended July 3, 2005 and June 27, 2004. The

diluted earnings per share calculation excluded 0.4 million and 91 million shares related to options for the fiscal second quarters ended July 3, 2005 and June 27, 2004, respectively, as the exercise price per share of these options was greater than the average market value. If these shares were included it would result in an anti-dilutive effect on diluted earnings per share. The following is a reconciliation of basic net earnings per share to diluted net earnings per share for the fiscal six months ended July 3, 2005 and June 27, 2004. (Shares in Millions) Fiscal Six Months Ended July 3, June 27, 2005 2004 Basic net earnings per share $ 1.88 1.67 Average shares outstanding - basic 2,973.0 2,968.1 Potential shares exercisable under stock option plans 214.3 152.7 Less: shares which could be repurchased under treasury stock method (172.9) (131.2) Convertible debt shares 7.4 14.8 Average shares outstanding - diluted 3,021.8 3,004.4 Diluted earnings per share $ 1.86 1.65 The diluted earnings per share calculation included the dilutive effect of convertible debt that was offset by the related reduction in interest expense of $7 million for the first fiscal six months ended July 3, 2005 and June 27, 2004, respectively. The diluted earnings per share calculation excluded 46 million and 92 million shares related to options for the first fiscal six months ended July 3, 2005 and June 27, 2004, respectively, as the exercise price per share of these options was greater than the average market value. If these shares were included it would result in an anti-dilutive effect on diluted earnings per share. NOTE 8 - ACCUMULATED OTHER COMPREHENSIVE INCOME The total comprehensive income for the first fiscal six months ended July 3, 2005 was $5.3 billion, compared with $5.0 billion for the same period a year ago. The total comprehensive income for the fiscal second quarter ended July 3, 2005 was $2.5 billion, which is unchanged from the same period a year ago. Total comprehensive income included net earnings, net unrealized currency gains and losses on translation, net unrealized gains and losses on available for sale securities and net gains and losses on derivative instruments qualifying and designated as cash flow hedges. The following table sets forth the components of accumulated other comprehensive income. 15 Total Unrld Gains/ Accum For. Gains/ Pens (Losses) Other Cur. (Losses) Liab on Deriv Comp Trans. on Sec Adj. & Hedg Inc/ (Loss) January 2, 2005 $ (105) 86 (346) (150) (515) 2005 six months changes: Net change associated with current period hedging transactions - - - 402 Net amount reclassed to net earnings - - - (317)* Net six months changes (343) (32) - 85 (290) July 3, 2005 $ (448) 54 (346) (65) (805) Amounts in accumulated other comprehensive income are presented net of the related tax impact. Foreign currency translation adjustments are not currently adjusted for income taxes, as they relate to permanent investments in international subsidiaries. *Primarily offset in net earnings by changes in value of the underlying transactions. NOTE 9 - MERGERS, ACQUISITIONS AND DIVESTITURES On December 15, 2004, Johnson & Johnson announced the signing of a definitive agreement to acquire Guidant Corporation (Guidant), a world leader in the treatment of cardiac and vascular disease, for $25.4 billion in fully diluted equity value. The Boards of Directors of Johnson & Johnson and Guidant, as well as the shareholders of Guidant have given their respective approvals for the transaction. The transaction is subject to clearance under the Hart- Scott-Rodino Antitrust Improvements Act, the European Union merger control regulation, and other customary closing conditions. The Company is currently in the process of responding to an information and materials request from the U.S. Federal Trade Commission and has entered into a second phase review with the European Union. In addition, the Company is engaged in discussions with Guidant to help the Company understand the issues surrounding the recent product notifications and product recalls. The Company continues to work toward a fiscal third quarter close of the acquisition, which is subject to the outcome of the previously mentioned activities. On April 4, 2005 the Company completed its acquisition of TransForm Pharmaceuticals, Inc., a company specializing in the discovery of superior formulations and novel crystalline forms of drug molecules, for $230 million. During the fiscal second quarter of 2005 a one-time before and after- tax charge of $50 million reflecting the expensing of IPR&D charges was incurred. On June 3, 2005 the Company completed its acquisition of CLOSURE Medical, a company with expertise and intellectual property in the 16 biosurgicals market, for a net purchase price of $364 million. During the fiscal second quarter of 2005 a one-time before and after-tax charge of approximately $51 million reflecting the expensing of IPR&D charges was incurred. On June 30, 2005 the Company completed its acquisition of Peninsula Pharmaceuticals, Inc., a privately held biopharmaceutical company focused on developing and commercializing antibiotics to treat life-threatening infections, for a purchase price of approximately $245 million. During the fiscal second quarter of 2005, a one-time before and after-tax charge of approximately $252 million reflecting the expensing of IPR&D charges was incurred. The Company's 2004 acquisitions included: Merck's 50% interest in the Johnson & Johnson-Merck Consumer Pharmaceuticals Co. European non-prescription pharmaceutical joint venture including all of the infrastructure and brand assets managed by the European joint venture; Egea Biosciences, Inc., which has developed a proprietary technology platform called Gene Writer, that allows for the rapid and highly accurate synthesis of DNA sequences, gene assembly, and construction of large synthetic gene libraries, through the exercise of the option to acquire the remaining outstanding stock not owned by Johnson & Johnson; Artemis Medical, Inc. a privately held company with ultrasound and x-ray visible biopsy site breast markers as well as hybrid markers; U.S. commercial rights to certain patents and know-how in the field of sedation and analgesia from Scott Lab, Inc.; Biapharm SAS, a privately held French producer and marketer of skin care products centered around the leading brand BIAFINE(r); the assets of Micomed, a privately owned manufacturer of spinal implants primarily focused on supplying the German market; and the acquisition of the AMBI skin care brand for women of color. NOTE 10 - PRO FORMA STOCK BASED COMPENSATION At July 3, 2005, the Company had 18 stock-based employee compensation plans. The Company accounts for those plans under the recognition and measurement principles of Accounting Principle Board Opinion No. 25 "Accounting for Stock Issued to Employees" and its related Interpretations. Compensation costs were not recorded in net income for stock options, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. As required by SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure - an amendment of FASB Statement No. 123," the following table shows the estimated effect on net income and earnings per share if the Company had applied the fair value recognition provision of SFAS No. 123, "Accounting for Stock-Based Compensation," to stock- based employee compensation. (Dollars in Millions 17 Except Per Share Data) Fiscal Second Quarter Ended July 3, 2005 June 27, 2004 Net income, as reported $ 2,676 2,458 Less: Compensation expense(1) 88 88 Net Income,pro forma $ 2,588 2,370 Earnings per share: Basic - as reported $.90 $.83 - pro forma .87 .80 Diluted - as reported $.89 $.82 - pro forma .86 .79 (1) Determined under fair value based method for all awards, net of tax. (Dollars in Millions Except Per Share Data) Fiscal Six Months ended July 3, 2005 June 27, 2004 Net income, as reported $ 5,603 4,951 Less: Compensation expense(1) 176 166 Net Income, pro forma $ 5,427 4,785 Earnings per share: Basic - as reported $1.88 $1.67 - pro forma 1.83 1.61 Diluted - as reported $1.86 $1.65 - pro forma 1.80 1.59 (1) Determined under fair value based method for all awards, net of tax. NOTE 11 - PENSIONS AND OTHER POSTRETIREMENT BENEFITS Components of Net Periodic Benefit Cost Net periodic benefit cost for the Company's defined benefit retirement plans and other benefit plans for the fiscal second quarters of 2005 and 2004 include the following components: (Dollars in Millions) Retirement Plans Other Benefit Plans Fiscal Second Quarter ended July 3, June 27, July 3, June 27, 2005 2004 2005 2004 Service cost $ 106 104 15 11 Interest cost 128 106 18 25 Expected return on

plan assets (159) (127) (1) - Amortization of prior service cost 3 3 (2) - Amortization of net transition asset - - - - Recognized actuarial 18 losses 54 59 2 11 Net periodic benefit cost $ 132 145 32 47 Net periodic benefit cost for the Company's defined benefit retirement plans and other benefit plans for the first fiscal six months of 2005 and 2004 include the following components: (Dollars in Millions) Retirement Plans Other Benefit Plans Fiscal Six Months ended July 3, June 27, July 3, June 27, 2005 2004 2005 2004 Service cost $ 216 212 28 24 Interest cost 246 225 44 51 Expected return on plan assets (291) (258) (2) (1) Amortization of prior service cost 6 7 (3) (1) Amortization of net transition asset (1) (1) - - Recognized actuarial losses 111 103 13 22 Net periodic benefit cost $ 287 288 80 95 Company Contributions As of July 3, 2005, the Company contributed $11 million and $23 million to its U.S. and international retirement plans, respectively, in 2005. The Company does not anticipate a minimum statutory funding requirement for its U.S. retirement plans in 2005. However the Company may or may not choose to further fund the plans in 2005. International plans will be funded in accordance with local regulations. NOTE 12 - LEGAL PROCEEDINGS Product Liability The Company is involved in numerous product liability cases in the United States, many of which concern adverse reactions to drugs and medical devices. The damages claimed are substantial, and while the Company is confident of the adequacy of the warnings and instructions for use that accompany such products, it is not feasible to predict the ultimate outcome of litigation. However, the Company believes that if any liability results from such cases, it will be substantially covered by existing amounts accrued in the Company's balance sheet under its self- insurance program and by third-party product liability insurance. One group of cases against the Company concerns the Janssen Pharmaceutica Inc. ("Janssen") product PROPULSID (cisapride), which was withdrawn from general sale and restricted to limited use in 2000. In the wake of publicity about those events, numerous 19 lawsuits were filed against Janssen and the Company regarding PROPULSID in state and federal courts across the country. These actions seek substantial compensatory and punitive damages and accuse Janssen and the Company of inadequately testing for and warning about the drug's side effects, of promoting it for off-label use and over promotion. In addition, Janssen and the Company have entered into tolling agreements with various plaintiffs' counsel halting the running of the statutes of limitations with respect to the potential claims of a significant number of individuals while those attorneys evaluate whether or not to sue Janssen and the Company on their behalf. On February 5, 2004, Janssen announced that it had reached an agreement in principle with the Plaintiffs Steering Committee (PSC) of the PROPULSID Federal Multi-District Litigation (MDL), to resolve federal lawsuits related to PROPULSID. The agreement was to become effective once 85% of the death claimants, and 75% of the remainder, agreed to the terms of the settlement. In addition, 12,000 individuals who had not filed lawsuits, but whose claims were the subject of tolling agreements suspending the running of the statutes of limitations against those claims, also had to agree to participate in the settlement before it became effective. On March 24, 2005, it was confirmed that the PSC of the MDL had enrolled enough plaintiffs and claimants in the settlement program to make the agreement effective. Of the 282 death plaintiffs subject to the program, 247 (88%) are confirmed enrolled. Of the 3,543 other plaintiffs subject to the program, 3,082 (87%) are confirmed enrolled. In addition, 19,788 "tolled" claimants are confirmed as enrolled. Those participating in the settlement will submit medical records to an independent panel of physicians who will determine whether the claimed injuries were caused by PROPULSID and otherwise meet the standards for compensation. If those standards are met, a court-appointed special master will determine compensatory damages. Janssen has paid into a compensation escrow account $72.3 million and could pay up to an additional $17.7 million depending on the number of plaintiffs that enroll in the program. Enrollment will remain open until October 1, 2005. Janssen has established an administrative fund of $15 million, and paid legal fees to the PSC of $22.5 million, which amount was approved by the court. Not participating in the settlement program are 2,547 plaintiffs and 7,843 tolled claimants. Of those, 453 plaintiffs are potentially subject to the MDL settlement but have not to date enrolled in it; 1,532 plaintiffs filed cases in federal court subsequent to February 1, 2004, and thus are not subject to the MDL settlement; and 562 have state court actions and thus are not subject to the settlement. Of those not participating in or subject to the MDL settlement, 159 plaintiffs are alleged to have died from use of the drug and 2,388 assert other personal injury claims. The nature of the claims of the tolled claimants are unknown. Of the remaining federal and state plaintiffs, 2,254 cases (89%) are venued in Mississippi. 20 With respect to all the various PROPULSID actions against them, Janssen and the Company dispute the claims in those lawsuits and are vigorously defending against them except where, in their judgment, settlement is appropriate. Janssen and the Company believe they have adequate self-insurance accruals and third-party product liability insurance with respect to these cases. In communications to the Company, the excess insurance carriers have raised certain defenses to their liability under the policies and to date have declined to reimburse Janssen and the Company for PROPULSID-related costs despite demand for payment. In May 2005, hearings were held in London in the arbitration proceeding commenced by Janssen and the Company against Allianz Underwriters Insurance Company, which issued the first layer of applicable excess insurance coverage, to obtain reimbursement of PROPULSID-related costs. Final arguments in that matter were held on July 22, 2005 and a decision is expected before the end of 2005. In May 2005, the Company commenced arbitration against Lexington Insurance Company, which issued the second layer of excess insurance coverage. In the opinion of the Company, the excess carriers remain legally obligated to provide coverage for the PROPULSID-related losses at issue. The Company's Ethicon, Inc. ("Ethicon") subsidiary has over the last several years had a number of claims and lawsuits filed against it relating to VICRYL sutures. The actions allege that the sterility of VICRYL sutures was compromised by inadequacies in Ethicon's systems and controls, causing patients who were exposed to these sutures to incur infections that would not otherwise have occurred. Ethicon on several occasions recalled batches of VICRYL sutures in light of questions raised about sterility but does not believe any contamination of suture products in fact occurred. In November 2003, a state court judge in West Virginia certified for class treatment all West Virginia residents who had VICRYL sutures implanted during Class I or II surgeries from May 1, 1994 to December 31, 1997. A motion to decertify the class was granted on May 17, 2005. Ethicon has been and intends to continue vigorously defending against the claims. Affirmative Stent Patent Litigation In patent infringement actions tried in Delaware Federal District Court in late 2000, Cordis Corporation (Cordis), a subsidiary of Johnson & Johnson, obtained verdicts of infringement and patent validity, and damage awards against Boston Scientific Corporation (Boston Scientific) and Medtronic AVE, Inc. (Medtronic) based on a number of Cordis vascular stent patents. On December 15, 2000, the jury in the damage action against Boston Scientific returned a verdict of $324 million and on December 21, 2000, the jury in the Medtronic action returned a verdict of $271 million. These sums represent lost profit and reasonable royalty damages to compensate Cordis for infringement but do not include pre or post judgment interest. In February 2001 a hearing was held on the claims of Boston Scientific and Medtronic that the patents at issue were unenforceable owing to alleged inequitable conduct before the patent office. 21 In March and May 2002, the district judge issued post trial rulings that confirmed the validity and enforceability of the main Cordis stent patent claims but found certain other Cordis patents unenforceable. Further, the district judge granted Boston Scientific a new trial on liability and damages and vacated the verdict against Medtronic on legal grounds. On August 12, 2003, the Court of Appeals for the Federal Circuit found the trial judge erred in vacating the verdict against Medtronic

and remanded the case to the trial judge for further proceedings. In March 2005, the remaining issues were tried in the remanded case against Medtronic and the retrial proceeded against Boston Scientific. Juries returned verdicts of infringement and patent validity in favor of Cordis in both retrials. Cordis has requested the trial court to reinstate with interest the verdicts obtained against those entities in 2000. Defendants in both cases have filed post-trial motions seeking to vacate the jury verdicts or, alternatively, grant them a new trial on damages. Cordis also has pending in Delaware Federal District Court a second action against Medtronic AVE accusing Medtronic of infringement by sale of stent products introduced by Medtronic subsequent to its GFX and MicroStent products, the subject of the earlier action referenced above. That second action was stayed in April 2005 pending the outcome of an arbitration concerning Medtronic's claim that the products at issue in that case are licensed pursuant to a 1997 license. In January 2003, Cordis filed a patent infringement action against Boston Scientific in Delaware Federal District Court accusing its Express2, TAXUS and Liberte stents of infringing the Palmaz patent that expires in November 2005. The Liberte stent was also accused of infringing Cordis' Gray patent that expires in 2016. In June 2005, a jury found that the Express2, Taxus and Liberte stents infringed the Palmaz patent and that the Liberte stent also infringed the Gray patent. Boston Scientific will ask the trial judge to vacate the verdicts and, if unsuccessful, there will be a trial on damages and willfulness in the future. Patent Litigation Against Various Johnson & Johnson Subsidiaries The products of various Johnson & Johnson subsidiaries are the subject of various patent lawsuits, the outcomes of which could potentially adversely affect the ability of those subsidiaries to sell those products, or require the payment of past damages and future royalties. With respect to all of these matters, the Johnson & Johnson subsidiary involved is vigorously defending against the claims of infringement and disputing where appropriate the validity and enforceability of the patent claims asserted against it. On July 1, 2005, a jury in Federal District Court in Delaware found that the Cordis Cypher stent infringed Boston Scientific's Ding `536 patent and that the Cordis Cypher and Bx Velocity stents also infringed Boston Scientific Corporation's Jang `021 patent. The jury also found both those patents valid. Cordis will ask the judge to overturn the jury verdicts or grant a new trial. If the judge does not overturn the jury verdicts, there will be a damage 22 and willfulness trial in 2006 and Boston Scientific will seek an injunction against Cypher. If upheld by the trial court, Cordis will appeal the jury verdicts to the Court of Appeals for the Federal Circuit. In November 2005, Boston Scientific's case asserting infringement by the Cypher stent of another Boston Scientific patent is scheduled for trial in Delaware Federal District Court. In that case as well, Boston Scientific seeks an injunction and substantial damages. On January 26, 2005, the Federal District Court for the Southern District of Florida granted Cordis summary judgment dismissing a breach of contract and patent infringement suit filed against Cordis by Arlaine and Gina Rockey seeking royalties on the sales of all Cordis balloon expandable stents. Plaintiffs have filed an appeal with the Court of Appeals for the Federal Circuit. On June 8, 2005, in an action brought by Boston Scientific against Cordis in the Netherlands under the Kastenhofer patent, Cordis was enjoined from manufacturing and selling in the Netherlands two-layer catheters, including those used with the Cypher Stent. The injunction was stayed by another Dutch court. This stay decision is being appealed by Boston Scientific. In any event, Cordis does not anticipate a disruption in the supply of Cypher product outside the Netherlands, even if the injunction becomes effective. The following chart summarizes various patent lawsuits concerning products of Johnson & Johnson subsidiaries. Product J&J Patents Plaintiff/Patent Court Trial Date Company Holder Date Filed Drug Cordis Ding Boston Scientific Germany TBD 02/04 Eluting Corp. Stents Drug Cordis Grain- Boston Scientific D.Del. 10/05 12/03 Eluting ger Corp. Stents Stents Cordis Boneau Medtronic Inc. Arbitration TBD 4/02 Two-layer Cordis Kasten- Boston Scientific N.D.Cal. TBD 2/02 Catheters hofer Corp. Netherlands 04/05 05/04 Forman Belgium 10/05 12/03 S.D. Cal TBD 02/02 Remicade Centocor Cerami Rockefeller E.D.Tex. 2/06 04/04 University and Chiron Corporation Stents Cordis Israel Medinol Multiple TBD 05/03 E.U. Contact Vision Nicolson CIBA Vision M.D. Fla. TBD 09/03 Lenses Care Trocars Ethicon Hart Applied Medical C.D. Cal. 10/05 9/03 Endo Resources 23 Litigation Against Filers of Abbreviated New Drug Applications (ANDAs) The following chart indicates lawsuits pending against generic firms that filed Abbreviated New Drug Applications seeking to market generic forms of products sold by various subsidiaries of the Company prior to expiration of the applicable patents covering those products. These ANDAs typically include allegations of non-infringement, invalidity and unenforceability of these patents. In the event the subsidiary of the Company involved is not successful in these actions, or the 30-month stay expires before a ruling from the district court is obtained, the firms involved will have the ability to introduce generic versions of the product at issue resulting in very substantial market share and revenue losses for the product of the Company's subsidiary. Brand Name Patent/NDA Generic Court Trial Date 30- Product Holder Challenger Date Filed Month Stay Expires Aciphex 20 mg Eisai Teva S.D.N.Y. TBD 11/03 02/07 delay release tablet (for Dr. Reddy's S.D.N.Y. TBD 11/03 02/07 Janssen) Mylan S.D.N.Y. TBD 01/04 02/07 Ditropan XL 5, Ortho- Mylan D.W.V. 2/05 05/03 09/05 10, 15 mg McNeil controlled ALZA Impax N.D.Cal. 12/05 09/03 01/06 release tablet Levaquin Daiichi, Mylan D.W.V. 05/04 02/02 07/04 Tablets 250, 500, 750 JJPRD mg tablets Ortho- Teva D.N.J. TBD 06/02 11/04 McNeil Levaquin Daiichi, Sicor (Teva) D.N.J. TBD 12/03 05/06 Injectable JJPRD Single use Ortho- vials and 5 McNeil mg/ml premix Levaquin Daiichi, American D.N.J. TBD 12/03 05/06 Injectable JJPRD Pharmaceutical Single use Ortho- Partners vials McNeil Quixin Daiichi, Hi-Tech D.N.J. TBD 12/03 05/06 Ophthalmic Pharmacal Solution (Levofloxacin) Ortho- Ophthalmic McNeil solution Ortho Tri- Ortho- Barr D.N.J. TBD 10/03 02/06 cyclen LO McNeil 0.18 mg/0.025 mg, 0.215 mg/0.025 mg and 0.25 mg/0.025 mg PEPCID Complete McNeil-PPC Perrigo S.D.N.Y. TBD 02/05 06/07 24 Razadyne Janssen Teva D. Del TBD 07/05 01/08 Mylan D. Del TBD 07/05 01/08 Dr. Reddy's D. Del TBD 07/05 01/08 Purepac D. Del TBD 07/05 01/08 Barr D. Del TBD 07/05 01/08 Par D. Del TBD 07/05 01/08 AlphaPharm D. Del TBD 07/05 01/08 Risperdal Janssen Mylan D.N.J. TBD 12/03 05/06 Tablets .25, 0.5, 1, 2, Dr. Reddy's D.N.J. TBD 12/03 06/06 3, 4 mg tablets Risperdal M-Tab Janssen Dr. Reddy's D.N.J. TBD 02/05 07/07 0.5, 1, 2 mg Sporanox Janssen Eon Labs E.D.N.Y. 5/04 04/01 03/04 100 mg capsule Topamax Ortho- Mylan D.N.J. TBD 04/04 09/06 McNeil 25, 100, 200 mg tablet Ultracet 37.5 Ortho-Kali (Par) D.N.J. TBD 11/02 04/05 tram/ McNeil 325 apap tablet Teva D.N.J. TBD 02/04 07/06 Caraco E.D. Mich. 03/06 09/04 02/07 In the action against Mylan involving Ortho McNeil's DITROPAN XL (oxybutynin chloride), the court held a ten-day bench trial, which concluded on April 18, 2005. A decision is expected in the third or fourth quarter of 2005. In the action against Mylan Pharmaceuticals USA (Mylan) involving Ortho-McNeil Pharmaceutical, Inc. (Ortho-McNeil) for LEVAQUIN (levofloxacin), the trial judge on December 23, 2004 found the patent at issue valid, enforceable and infringed by Mylan's contemplated ANDA product and issued an injunction precluding sale of the product until patent expiration in late 2010. Mylan has appealed to the Court of Appeals for the Federal Circuit. In the action against Eon Labs (Eon) involving Janssen's SPORANOX (itraconazole), the district court ruled on July 28, 2004 that Janssen's patent was valid but not infringed by Eon's generic. The Court of Appeals for the Federal Circuit affirmed the district court's decision on June 13, 2005. Eon Labs launched its generic product in February 2005. In the action against Mylan relating to Ortho- McNeil's TOPAMAX (topiramate), Mylan on October 8, 2004 filed a motion for summary judgment of non- infringement of Ortho-McNeil's patent. The court denied Mylan's motion on July 18, 2005. 25 In the action against Kali involving Ortho-McNeil's ULTRACET

(tramadol hydrochloride/ acetaminophen), Kali moved for summary judgment on the issues of infringement and invalidity. The briefing on that motion was completed in October 2004 and a decision is expected anytime. With respect to claims other than that at issue in the litigation against Kali, Ortho-McNeil has filed a reissue application in the U.S. Patent and Trademark Office seeking to narrow the scope of the claims. Kali received final approval of its ANDA at expiration of the 30-month stay on April 21, 2005, and launched its generic product the same day. If Ortho-McNeil ultimately prevails in its patent infringement action against Kali, Kali will be subject to an injunction and damages. In the action against Teva Pharmaceuticals USA (Teva) involving Ortho-McNeil's ULTRACET (tramadol hydrocholoride/ acetaminophen), Teva has moved for summary judgment on the issues of infringement and validity. The briefing on that motion was completed in March 2005. With respect to all of the above matters, the Johnson & Johnson subsidiary involved is vigorously defending the validity and enforceability and asserting the infringement of its own or its licensor's patents. Average Wholesale Price (AWP) Litigation Johnson & Johnson and its pharmaceutical subsidiaries, along with numerous other pharmaceutical companies, are defendants in a series of lawsuits in state and federal courts involving allegations that the pricing and marketing of certain pharmaceutical products amounted to fraudulent and otherwise actionable conduct because, among other things, the companies allegedly reported an inflated Average Wholesale Price (AWP) for the drugs at issue. Most of these cases, both federal actions and state actions removed to federal court, have been consolidated for pre-trial purposes in a Multi- District Litigation (MDL) in federal district court in Boston, Massachusetts. The plaintiffs in these cases include classes of private persons or entities that paid for any portion of the purchase of the drugs at issue based on AWP, and state government entities that made Medicaid payments for the drugs at issue based on AWP. In the MDL proceeding in Boston, plaintiffs have moved for class certification of all or some portion of their claims. A decision is expected on that motion in the third or fourth quarter of 2005. Ethicon Endo-Surgery, Inc. ("Ethicon Endo"), a Johnson & Johnson subsidiary which markets endoscopic surgical instruments, and the Company, are named defendants in a North Carolina state court class action lawsuit alleging AWP inflation and improper marketing activities against TAP Pharmaceuticals. Ethicon Endo is a defendant based on claims that several of its former sales representatives are alleged to have been involved in arbitrage of a TAP drug. The allegation is that these sales representatives persuaded certain physicians in states where the drug's price was low to purchase from TAP excess quantities of the drug and then resell it in states where its price was higher. Ethicon Endo and the Company deny any liability for the claims made against them in this case and are vigorously defending against it. On April 24, 26 2003, the trial judge certified a national class of purchasers of the TAP product at issue. On July 6, 2004, that class was decertified by the North Carolina Court of Appeals and the matter remanded to the trial court for additional consideration. On January 5, 2005, the trial judge certified a North Carolina State class of purchasers of the TAP product in question. No trial date has been set in this matter. Other The New York State Attorney General's office (N.Y. AG) and the Federal Trade Commission issued subpoenas in January and February 2003 seeking documents relating to the marketing of sutures and endoscopic instruments by the Company's Ethicon and Ethicon Endo subsidiaries. In February 2005, the N.Y. AG advised that it had closed its investigation. The Connecticut State Attorney General's office also issued a subpoena for the same documents. These subpoenas focus on the bundling of sutures and endoscopic instruments in contracts offered to Group Purchasing Organizations and individual hospitals in which discounts are predicated on the hospital achieving specified market share targets for both categories of products. The operating companies involved have responded to the subpoenas. On June 26, 2003, the Company received a request for records and information from the U.S. House of Representatives' Committee on Energy and Commerce in connection with its investigation into pharmaceutical reimbursements and rebates under Medicaid. The Committee's request focuses on the drug REMICADE (infliximab), marketed by the Company's Centocor, Inc. ("Centocor") subsidiary. On July 2, 2003, Centocor received a request that it voluntarily provide documents and information to the criminal division of the U.S. Attorney's Office, District of New Jersey, in connection with its investigation into various Centocor marketing practices. Subsequent requests for documents have been received from the U.S. Attorney's Office. Both the Company and Centocor responded, or are in the process of responding, to these requests for documents and information. On August 1, 2003, the Securities and Exchange Commission (SEC) advised the Company of its informal investigation under the Foreign Corrupt Practices Act of allegations of payments to Polish governmental officials by U.S. pharmaceutical companies. On November 21, 2003, the SEC advised the Company that the investigation had become formal and issued a subpoena for the information previously requested in an informal fashion, in addition to other background documents. The Company and its operating units in Poland have responded to these requests. On December 8, 2003, Ortho-McNeil, a subsidiary of Johnson & Johnson, received a subpoena from the United States Attorney's Office in Boston, Massachusetts seeking documents relating to the marketing, including alleged off-label marketing, of the drug TOPAMAX (topiramate). Ortho-McNeil is cooperating in responding to the subpoena. In October 2004, the U.S. Attorney's Office in Boston asked attorneys for Ortho-McNeil to cooperate in 27 facilitating the subpoenaed testimony of several present and former Ortho-McNeil employees before a grand jury in Boston. Cooperation in securing the testimony of additional witnesses before the grand jury has been requested and is being provided. On January 20, 2004, the Company's subsidiary, Janssen, received a subpoena from the Office of the Inspector General of the United States Office of Personnel Management seeking documents concerning sales and marketing of, any and all payments to physicians in connection with sales and marketing of, and clinical trials for, RISPERDAL (risperidone) from 1997 to 2002. Documents subsequent to 2002 have also been requested. Janssen is cooperating in responding to the subpoena. In April 2004, the Company's pharmaceutical companies were requested to submit information to the U.S. Senate Finance Committee on their use of the "nominal pricing exception" in calculating Best Price under the Medicaid Rebate Program. This request was sent to manufacturers for the top twenty drugs reimbursed under the Medicaid Program. The Company's pharmaceutical companies have responded to the request. In February 2005 a request for supplemental information was received from the Senate Finance Committee, which has been responded to by the Company's pharmaceutical companies. On July 27, 2004, the Company received a letter request from the New York State Attorney General's Office for documents pertaining to marketing, off- label sales and clinical trials for TOPAMAX (topiramate), RISPERDAL (risperidone), PROCRIT (Epoetin alfa), REMINYL (galantamine HBr), REMICADE (infliximab) and ACIPHEX (rabeprazole sodium). The Company is responding to the request. On August 9, 2004, Johnson & Johnson Health Care Systems, Inc. (HCS), a Johnson & Johnson subsidiary, received a subpoena from the Dallas, Texas U. S. Attorney's Office seeking documents relating to the relationships between the group purchasing organization Novation and HCS and other Johnson & Johnson subsidiaries. The Company's subsidiaries involved are responding to the subpoena. On September 30, 2004, Ortho Biotech Inc. ("Ortho Biotech"), a Johnson & Johnson subsidiary, received a subpoena from the U.S. Office of Inspector General's Denver, Colorado field office seeking documents directed to sales and marketing of PROCRIT (Epoetin alfa) from 1997 to the present. Ortho Biotech is responding to the subpoena. In March 2005, DePuy Orthopaedics, Inc. ("DePuy"), a Johnson & Johnson subsidiary, received a subpoena from the U.S. Attorney's Office, District of New Jersey, seeking records concerning contractual relationships

between DePuy and surgeons or surgeons in training involved in hip and knee replacement and reconstructive surgery. Other leading orthopaedic companies are known to have received the same subpoena. DePuy is responding to the subpoena. 28 On June 9, 2005, The United States Senate Committee on Finance requested the Company to produce information regarding its use of educational grants. A similar request was sent to other major pharmaceutical companies. On July 5, 2005, the Committee specifically requested information about educational grants in connection with the drug PROPULSID. The Company is in the process of responding to the request. On July 20, 2005, Scios, Inc. ("Scios"), a Johnson & Johnson subsidiary, received a subpoena from the United States Attorney's Office, District of Massachusetts, seeking documents related to the sales and marketing of NATRECOR. Scios is responding to the subpoena. In early August 2005, Scios was advised that the investigation will be handled by the United States Attorney's Office for the Northern District of California in San Francisco, rather than the United States Attorney's Office in Boston, Massachusetts. In September 2004, plaintiffs in an employment discrimination litigation initiated against the Company in 2001 in Federal District Court in New Jersey moved to certify a class of all African American and Hispanic salaried employees of the Company and its affiliates in the United States, who were employed at any time from November 1997 to the present. Plaintiffs seek monetary damages for the period 1997 through the present (including punitive damages) and equitable relief. The Company filed its response to plaintiffs' class certification motion in May 2005. A decision by the District Court is not expected until 2006. The Company disputes the allegations in the lawsuit and is vigorously defending against them. The Company, along with its wholly owned Ethicon and Ethicon-Endo subsidiaries, are defendants in three federal antitrust actions challenging suture and endo- mechanical contracts with Group Purchasing Organizations and hospitals in which discounts are predicated on a hospital achieving specified market share targets for both categories of products. In each case, plaintiffs seek substantial monetary damages and injunctive relief. In Applied Medical v. Ethicon Inc. et al (C.D.CA, filed September 5, 2003), fact discovery is complete and the defendants have moved for summary judgment on all claims. In Conmed v. Johnson & Johnson et al (S.D.N.Y., filed November 6, 2003), fact discovery is also complete and summary judgment motions are due September 30, 2005. In Genico v. Ethicon, Inc. et al (E.D. TX, filed October 15, 2004) written discovery is underway. After a remand from the Federal Circuit Court of Appeals in January 2003, a partial retrial was commenced in October and concluded in November 2003 in Federal District Court in Boston, Massachusetts in the action Amgen v. Transkaryotic Therapies, Inc. (TKT) and Aventis Pharmaceutical, Inc. (Aventis). The matter is a patent infringement action brought by Amgen against TKT, the developer of a gene-activated EPO product, and Aventis, which held marketing rights to the TKT product, asserting that TKT's product infringes various Amgen, Inc. (Amgen) patent claims. TKT and Aventis dispute infringement and are seeking to invalidate the Amgen patents asserted against them. On October 15, 2004, the district court issued rulings that upheld its initial findings in 2001 that Amgen's patent claims were valid and infringed. Further proceedings and an appeal will follow. The Amgen patents at issue 29 in the case are exclusively licensed to Ortho Biotech Inc. in the U.S. for non-dialysis indications. Ortho Biotech Inc. is not a party to the action. The Company is also involved in a number of other patent, trademark and other lawsuits incidental to its business. The ultimate legal and financial liability of the Company in respect to all claims, lawsuits and proceedings referred to above cannot be estimated with any certainty. However, in the Company's opinion, based on its examination of these matters, its experience to date and discussions with counsel, the ultimate outcome of legal proceedings, net of liabilities already accrued in the Company's balance sheet, is not expected to have a material adverse effect on the Company's financial position, although the resolution in any reporting period of one or more of these matters could have a significant impact on the Company's results of operations and cash flows for that period. Item 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS Results of Operations Analysis of Consolidated Sales For the first fiscal six months of 2005, worldwide sales were $25.6 billion, an increase of 11.1% over 2004 first fiscal six month sales of $23.0 billion. The impact of foreign currencies accounted for 2.1% of the total reported fiscal six month increase. Sales by U.S. companies were $14.3 billion in the first fiscal six months of 2005, which represented an increase of 5.4% over the same period last year. Sales by international companies were $11.3 billion, which represented an increase of 19.2%, of which 5.1% was due to currency fluctuations. All international regions throughout the world posted double digit sales increases during the first fiscal six months of 2005 as sales increased 16.0% in Europe, 21.2% in the Western Hemisphere (excluding the U.S.) and 24.7% in the Asia-Pacific, Africa region. These sales gains included the positive impact of currency fluctuations between the U.S. dollar and foreign currencies in Europe of 5.3%, in the Western Hemisphere (excluding the U.S.) of 8.1% and in the Asia-Pacific, Africa region of 3.4%. For the fiscal second quarter of 2005, worldwide sales were $12.8 billion, an increase of 11.1% over 2004 fiscal second quarter sales of $11.5 billion. The impact of foreign currencies accounted for 2.0% of the total reported fiscal second quarter 2005 increase. Sales by U.S. companies were $7.1 billion in the fiscal second quarter of 2005, which represented an increase of 6.0%. Sales by international companies were $5.7 billion, which represented an increase of 18.3%, of which 4.9% was due to positive currency fluctuations. 30 All international regions throughout the world posted double digit sales increases during the fiscal second quarter of 2005 as sales increased 14.6% in Europe, 20.7% in the Western Hemisphere (excluding the U.S.) and 24.4% in the Asia-Pacific, Africa region. These sales gains included the positive impact of currency fluctuations between the U.S. dollar and foreign currencies in Europe of 4.6%, in the Western Hemisphere (excluding the U.S.) of 10.0% and in the Asia-Pacific, Africa region of 3.1%. Analysis of Sales by Business Segments Consumer Consumer segment sales in the first fiscal six months of 2005 were $4.6 billion, an increase of 12.6% over the same period a year ago with 10.0% of operational growth and a positive currency impact of 2.6%. U.S. Consumer segment sales increased by 6.7% while international sales gains of 18.8% included a positive currency impact of 5.4%. Major Consumer Franchise Sales - First Fiscal Six Months Total Operations Currency 2005 2004 %Change %Change %Change OTC Pharm & Nutr. $ 1,313 $ 1,096 19.8% 18.2% 1.6% Skin Care 1,223 1,071 14.2 11.2 3.0 Women's Health 782 716 9.2 5.9 3.3 Baby & Kids Care 772 703 9.8 6.7 3.1 Other 468 461 1.5 0.5 1.0 Total $ 4,558 $4,047 12.6% 10.0% 2.6% Consumer segment sales in the fiscal second quarter of 2005 were $2.3 billion, an increase of 13.9% over the same period a year ago with 11.1% of operational growth and a positive currency impact of 2.8%. U.S. Consumer segment sales increased by 10.6% while international sales gains of 17.1% included a positive currency impact of 5.5%. Major Consumer Franchise Sales - Fiscal Second Quarter Total Operations Currency 2005 2004 %Change %Change %Change OTC Pharm & Nutr. $ 628 $ 532 18.0% 15.7% 2.3% Skin Care 602 509 18.5 15.5 3.0 Women's Health 406 368 10.3 6.7 3.6 Baby & Kids Care 393 360 9.2 5.9 3.3 Other 249 231 7.8 5.9 1.9 Total $ 2,278 $ 2,000 13.9% 11.1% 2.8% Consumer segment sales growth in the fiscal second quarter was attributable to strong sales performance in the major franchises in this segment including OTC Pharmaceutical & Nutritional products, Skin Care, Women's Health and Baby & Kids Care. OTC 31 Pharmaceutical & Nutritional operational sales growth of 15.7% was primarily driven by continued growth in SPLENDA(r) No Calorie Sweetener and pediatric analgesics. The Skin Care franchise operational sales growth of 15.5% was attributed to NEUTROGENA(r), AVEENO(r), RoC(r), CLEAN & CLEAR(r) and JOHNSON'S(r) adult brands. The key drivers of U.S. Skin Care growth were the continued

success with the NEUTROGENA(r) Advanced Solutions Microdermabrasion kit, along with new products launched in the first half of 2005. The Women's Health franchise achieved operational growth of 6.7% resulting from strong contributions from the K-Y(r) and STAYFREE(r) product lines. The Baby & Kids Care franchise operational sales growth of 5.9% resulted from continued success with JOHNSON'S(r) SOFTWASH(r) AND SOFTLOTION(r) product lines. Pharmaceutical Pharmaceutical segment sales in the first fiscal six months of 2005 were $11.4 billion, an increase of 5.4% over the same period a year ago with 3.8% of this change due to operational increases and the remaining 1.6% increase related to the positive impact of currency. The U.S. Pharmaceutical sales increase was 1.3% and the growth in international Pharmaceutical sales was 13.9% which included 5.1% related to the positive impact of currency. Major Pharmaceutical Product Revenues - First Fiscal Six Months Total Operations Currency 2005 2004 %Change %Change %Change RISPERDAL(r) $1,738 $1,458 19.3% 16.9% 2.4% PROCRIT(r)/ EPREX(r) 1,682 1,852 (9.2) (10.8) 1.6 REMICADE(r) 1,219 1,003 21.5 21.5 0.0 TOPAMAX(r) 837 663 26.2 24.5 1.7 DURAGESIC(r)/ Fentanyl Transdermal 832 1,011 (17.8) (20.2) 2.4 LEVAQUIN(r)/ FLOXIN(r) 760 651 16.7 16.6 0.1 Hormonal Contraceptives 598 671 (10.5) (11.5) 1.0 Aciphex(r)/ Pariet(r) 559 510 9.5 6.7 2.8 Other 3,158 2,984 5.8 3.9 1.9 Total $11,383 $10,803 5.4% 3.8% 1.6% Pharmaceutical segment sales in the fiscal second quarter of 2005 were $5.6 billion, an increase of 3.7% over the same period a year ago with 2.1% of this change due to operational increases and the remaining 1.6% increase related to the positive impact of currency. The U.S. Pharmaceutical sales decrease was 1.3% and the growth in international Pharmaceutical sales was 14.0% which included 4.8% related to the positive impact of currency. Major Pharmaceutical Product Revenues - Fiscal Second Quarter Total Operations Currency 2005 2004 %Change %Change %Change RISPERDAL(r) $894 $727 23.0% 20.8% 2.2% PROCRIT(r)/ EPREX(r) 846 875 (3.4) (5.0) 1.6 REMICADE(r) 642 539 19.1 19.1 0.0 TOPAMAX(r) 431 335 28.6 27.0 1.6 DURAGESIC(r)/ 32 Fentanyl Transdermal 382 557 (31.5) (33.5) 2.0 LEVAQUIN(r)/ FLOXIN(r) 320 269 19.2 19.0 0.2 Hormonal Contraceptives 296 366 (19.2) (20.3) 1.1 Aciphex(r)/ Pariet(r) 281 263 7.0 4.3 2.7 Other 1,536 1,496 2.7 0.1 2.6 Total $5,628 $5,427 3.7% 2.1% 1.6% Pharmaceutical segment sales growth in the second quarter of 2005 was led by strong performances from RISPERDAL(r), REMICADE(r), TOPAMAX(r) and LEVAQUIN(r). The discussion to follow correlates to the sequence of the chart above. Growth was fueled by the continued success of RISPERDAL(r) (risperidone), and RISPERDAL CONSTA(r) (risperidone), a long acting injection medication that treats the symptoms of schizophrenia, with operational growth of 20.8%. PROCRIT(r) (Epoetin alfa) and EPREX(r) (Epoetin alfa) performance continued to be adversely affected by competition. Combined these two products had an operational decline of 5.0% in the second quarter of 2005. Volume associated with share loss to competitive products was the primary driver of the decline. PROCRIT(r) pricing has stabilized in the second quarter of 2005. REMICADE(r) (infliximab), a biologic approved for the treatment of Crohn's disease, ankylosing spondylitis, and use in the treatment of rheumatoid arthritis experienced strong operational growth of 19.1% over prior year fiscal second quarter. Sales of TOPAMAX(r) (topiramate), which has been approved for adjunctive use in epilepsy, as well as for the prophylactic treatment of migraines, experienced strong operational growth of 27.0%, over prior year fiscal second quarter. In June of 2005 TOPAMAX(r) was also approved for use as an initial monotherapy in the treatment of epilepsy. DURAGESIC(r) (fentanyl transdermal system) sales declined by 33.5% operationally, which was primarily driven by the negative impact of generic competition in the U.S. beginning in January 2005. An authorized generic version of DURAGESIC(r) being marketed for the Company in the U.S. has captured a strong portion of the generic market. LEVAQUIN(r) (levofloxacin) achieved operational sales growth of 19.0% over prior year benefiting from the late respiratory infection season. The hormonal contraceptive franchise experienced an operational decline of 20.3%. Adjusted for the impact of the performance-based rebate allowances that benefited the second quarter of 2004, sales growth in the second quarter of 2005 was approximately 6.0%. The adjusted sales growth of 6.0% was the result of strong performances by ORTHO EVRA(r), the first contraceptive patch approved by the FDA, and ORTHO TRI-CYCLEN(r) LO (norgestimate/ethinyl estradiol), a low dose oral contraceptive, however this was partially offset by the impact of generic competition. CONCERTA(r) (methylphenidate HCL), a product for the treatment of attention deficit hyperactivity disorder, sales continued to grow 33 despite the lack of patent exclusivity in the U.S. At present, the FDA has not approved any generic version that is substitutable for CONCERTA(r). Abbreviated New Drug Applications (ANDAs) for generic versions of CONCERTA(r) are pending and may be approved at any time. Medical Devices and Diagnostics Medical Devices and Diagnostics segment sales in the first fiscal six months of 2005 were $9.7 billion, an increase of 17.8% over the same period a year ago with 15.4% of this change due to operational increases and the remaining 2.4% increase related to the positive impact of currency. The U.S. Medical Devices and Diagnostics sales increase was 12.0% and the growth in international Medical Devices and Diagnostics sales was 24.1% which included 5.0% related to the positive impact of currency. Major Medical Devices and Diagnostics Franchise Sales - First Fiscal Six Months Total Operations Currency 2005 2004 %Change %Change %Change CORDIS(r) $1,983 $1,541 28.6% 26.2% 2.4% DEPUY(r) 1,973 1,678 17.6 15.6 2.0 ETHICON(r) 1,587 1,397 13.6 10.3 3.3 ETHICON ENDO- SURGERY(r) 1,550 1,375 12.7 10.2 2.5 LIFESCAN(r) 975 820 18.8 16.6 2.2 Vision Care 833 731 13.9 11.8 2.1 ORTHO-CLINICAL DIAGNOSTICS(r) 721 619 16.5 14.6 1.9 Other 31 32 (3.1) (2.1) (1.0) Total $9,653 $8,193 17.8% 15.4% 2.4% Medical Devices and Diagnostics segment sales in the fiscal second quarter of 2005 were $4.9 billion, an increase of 19.7% over the same period a year ago with 17.4% of this change due to operational growth and the remaining 2.3% increase related to the positive impact of currency. The U.S. Medical Devices and Diagnostics sales increase was 16.7% and the growth in international Medical Devices and Diagnostics sales was 22.7% which included 4.6% related to the positive impact of currency. Major Medical Devices and Diagnostics Franchise Sales - Fiscal Second Quarter Total Operations Currency 2005 2004 %Change %Change %Change CORDIS(r) $1,014 $664 52.6% 50.0% 2.6% DEPUY(r) 980 839 16.9 15.0 1.9 ETHICON(r) 798 716 11.5 8.5 3.0 ETHICON ENDO- SURGERY(r) 785 710 10.6 8.3 2.3 LIFESCAN(r) 474 420 12.9 10.8 2.1 Vision Care 426 377 13.0 11.1 1.9 ORTHO-CLINICAL DIAGNOSTICS(r) 366 317 15.7 13.9 1.8 Other 13 14 (7.1) (6.1) (1.0) Total $4,856 $4,057 19.7% 17.4% 2.3% 34 Sales growth in the Medical Devices and Diagnostics segment was led by strong results experienced across the segment. The Cordis franchise was a major driver, with operational growth of 50.0%. The primary growth driver of the Cordis franchise was the CYPHER(r) Sirolimus-eluting Stent in both U.S. and international markets, with excellent growth in Japan. In addition, the Biosense Webster business also had a strong quarter with its navigational catheter line of products. In April and July of 2004, Cordis Cardiology Division of Cordis Corporation received warning letters from the FDA regarding Good Manufacturing Practice and Good Clinical Practice regulations. These observations followed post-approval site inspections completed in 2003 and early 2004 including sites involved in the production of the CYPHER(r) Sirolimus- eluting stent. In response to the warning letters, Cordis has made improvements to their quality system. The FDA has completed inspections of the three facilities involved in the April warning letter and Cordis has provided written responses to the recent inspection observations. The DePuy franchise's operational growth of 15.0% was primarily attributed to DePuy's orthopaedic joint reconstruction products including the hip and knee

product lines. Strong performance was also achieved in DePuy's spine unit and Mitek sports medicine products. Ethicon worldwide sales grew operationally by 8.5% from the same period in the prior year. Contributing to the strong results was the continued penetration of VICRYL(r) (polyglactin 910) Plus, an anti- bacterial coated suture, growth of DERMABOND(r), a liquid skin adhesive and continued adoption of a variety of niche products. The Ethicon Endo-Surgery franchise experienced operational growth of 8.3% over prior year. This growth was mainly driven by endocutter sales that include products used in performing bariatric procedures for the treatment of obesity, an important focus area for the franchise. HARMONIC SCALPEL(r) sales led by excellent results achieved with the recently introduced HARMONIC(r) ACE were also a significant source of growth in the quarter. The LifeScan franchise operational growth of 10.8% was a result of continued growth of U.S. sales, as well as strong growth in international markets. ONETOUCH(r) ULTRA, blood glucose meter, has been the key growth driver in this franchise. Vision Care franchise operational sales growth of 11.1% was led by the continued success of ACUVUE(r) ADVANCETM brand contact lenses with HYDRACLEARTM and 1-DAY ACUVUE(r). The Ortho-Clinical Diagnostics franchise reported operational growth of 13.9% over prior year, which was driven by its market penetration of the automated blood typing products, continued growth of the ECI product, and growth in the clinical chemistry sales driven by success with the Vitros(r) 5.1 FS instrument platform and the Vitros(r) 350 Chemistry System. 35 Cost of Products Sold and Selling, Marketing and Administrative Expenses Consolidated costs of products sold for the first fiscal six months of 2005 decreased to 27.3% from 28.3% of sales over the same period a year ago. The decrease resulted from cost improvement initiatives and improved gross margins in the Medical Devices & Diagnostics segment, primarily driven by lower manufacturing costs related to CYPHER(r) Sirolimus- eluting Stent, which more than offset an unfavorable product mix. The cost of products sold for the fiscal second quarter of 2005 was 27.5% of sales, which is consistent with the same period in prior year. During the quarter, unfavorable mix was offset by cost improvement initiatives and improved gross margins in the Medical Devices and Diagnostics segment. Consolidated selling, marketing and administrative expenses for the first fiscal six months of 2005 increased 12.1% over the same period a year ago. Consolidated selling, marketing and administrative expenses as a percent to sales for the first fiscal six months of 2005 were 32.1% versus 31.9% for the same period a year ago. Consolidated selling, marketing and administrative expenses for the fiscal second quarter of 2005 increased 13.0% over the same period a year ago. As a percent to sales, consolidated selling, marketing and administrative expenses were 32.8% versus 32.3% for the same period a year ago. Increases in the quarterly and six month periods were primarily associated with higher levels of advertising spend. Research & Development Research activities represent a significant part of the Company's business. These expenditures relate to the development of new products, improvement of existing products, technical support of products and compliance with governmental regulations for the protection of the consumer. Worldwide costs of research activities, for the first fiscal six months of 2005 were $2.8 billion, an increase of 24.4% over the same period a year ago. Research and development spending in the fiscal second quarter of 2005 was $1.5 billion, an increase of 25.8% over the fiscal second quarter of 2004. This increase is a reflection of the solid progress achieved in products in late stage development. In-Process Research & Development In the fiscal second quarter of 2005, the Company recorded In-process Research & Development (IPR&D) charges of $353 million before and after tax related to acquisitions in the Pharmaceutical and Medical Devices and Diagnostics segments. These acquisitions included TransForm Pharmaceuticals, Inc., Peninsula Pharmaceuticals, Inc. and CLOSURE Medical Corporation. Other (Income) Expense, Net Other (income) expense is the account where the Company records gains and losses related to the sale and write-down of certain equity securities of the Johnson & Johnson Development Corporation, losses on the disposal of fixed assets, currency gains & losses, minority interests, litigation settlements, as well as royalty income. 36 OPERATING PROFIT BY SEGMENT Consumer Segment Operating profit for the Consumer segment as a percent to sales in the first fiscal six months of 2005 was 19.2% versus 20.5% over the same period a year ago. Operating profit as a percent to sales in the fiscal second quarter of 2005 was 18.3% versus 19.1% over the same period a year ago. This decrease was due to increased investment spending in consumer promotions and advertising for the OTC Pharmaceutical and Nutritional franchise. Pharmaceutical Segment Operating profit for the Pharmaceutical segment as a percent to sales in the first fiscal six months of 2005 was 32.7% versus 38.8% over the same period a year ago. Operating profit as a percent to sales in the fiscal second quarter of 2005 was 28.2% versus 38.8% over the same period a year ago. For both periods operating profit was negatively impacted by increased research and development spending and IPR&D. IPR&D of $302 million reduced operating profit as a percent to sales by 2.7% and 5.3% for the first fiscal six months and the fiscal second quarter, respectively. Medical Devices and Diagnostics Segment Operating profit for the Medical Devices and Diagnostics segment as a percent to sales in the first fiscal six months of 2005 was 30.1% versus 25.9% over the same period a year ago. Operating profit as a percent to sales in the fiscal second quarter of 2005 was 29.0% versus 26.0% over the same period a year ago. The increase in 2005 was due to improved gross profit, resulting from cost reduction programs, lower manufacturing costs related to CYPHER(r) Sirolimus-eluting Stent and favorable product mix. Interest (Income) Expense Interest income increased in both the first fiscal six months and fiscal second quarter of 2005 as compared to the same periods a year ago. The increase reflected an improved cash position as well as higher rates of interest being earned on cash holdings. The cash balance including marketable securities at the end of the fiscal second quarter of 2005 was $13.2 billion, which was $2.4 billion higher than the same period a year ago. Interest expense decreased in both the first fiscal six months and fiscal second quarter of 2005 as compared to the same periods a year ago, resulting from lower average debt balances. Provision For Taxes on Income The worldwide effective income tax rates for the first fiscal six months of 2005 and 2004 were 24.9% and 28.6%, a decrease of 3.7%. Of this decrease, 1.9% was attributed to increases in taxable income in lower tax jurisdictions relative to taxable income in higher tax jurisdictions. The remaining net decrease of 1.8% was attributed to a one-time tax benefit partially offset by IPR&D, as described below. Acquisition related In-process Research & Development (IPR&D) charges of $353 million that are non- deductible for tax purposes were recorded in the fiscal second quarter of 2005. 37 The fiscal second quarter of 2005 included a benefit of $225 million, due to the reversal of a tax liability previously recorded during the fiscal fourth quarter of 2004, associated with a technical correction made to the American Jobs Creation Act of 2004, in May 2005. LIQUIDITY AND CAPITAL RESOURCES Cash Flows Cash generated from operations provided the major sources of funds for the growth of the business, including working capital, capital expenditures, acquisitions, share repurchases, dividends and debt repayments. In the first fiscal six months of 2005, cash flow from operations was $4.7 billion, a decrease of $0.1 billion over the same period a year ago. Investing activities provided $0.8 billion in the first fiscal six months of 2005, as compared to the usage of $1.9 billion during the same period a year ago. The increase in cash generated by investing activities was a result of higher sales activity of investment securities, partially offset by an increase in acquisitions. Net cash used by financing activities decreased by $0.2 billion primarily due to lower levels of debt retirement, partially offset by an increase in dividends and the repurchase of common stock. Dividends On April 28, 2005, the Board of Directors declared a regular cash dividend of $0.33 per share, payable on June 7, 2005 to shareholders of record as of May 17, 2005. This represented an

increase of 15.8% in the quarterly dividend rate and was the 43rd consecutive year of cash dividend increases. On July 18, 2005, the Board of Directors declared a regular cash dividend of $0.33 per share, payable on September 13, 2005 to shareholders of record as of August 23, 2005. The Company expects to continue the practice of paying regular cash dividends. OTHER INFORMATION New Accounting Standards In December 2004, the FASB issued SFAS No. 123(R), Share Based Payment. This statement establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods and services. It focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions (such as employee stock options and restricted stock units). The statement requires the measurement of the cost of employee services received in exchange for an award of equity instruments (such as employee stock options and restricted stock units) at fair value on the grant date. That cost will be recognized over the period during which an employee is required to provide services in exchange for the award (the requisite service period). On April 14, 2005 the SEC approved a new rule that delays the effective date of SFAS No. 123(R) for annual, rather than interim, periods that begin after June 15, 2005. As a result, the Company will adopt this statement in the first fiscal quarter of 2006. 38 The Company will implement SFAS 151, Inventory Costs, an amendment of ARB No. 43 and SFAS 153, Exchanges of Non-monetary Assets, an amendment of APB 29 in the first quarter of 2006 and the third quarter of 2005 respectively, as allowed by the Standards. The Company believes the adoption of these statements will not have a material effect on its results of operations, cash flows or financial position. The following recent accounting pronouncements became effective in 2004 and did not have a material impact on the Company's results of operations, cash flows or financial position. *EITF Issue 02-14: Whether an Investor should apply the Equity Method of Accounting to Investments other than Common Stock. *EITF Issue 04-1: Accounting for Preexisting Relationships between the Parties to a Business Combination. Economic and Market Factors Johnson & Johnson is aware that its products are used in an environment where, for more than a decade, policymakers, consumers and businesses have expressed concern about the rising cost of health care. Johnson & Johnson has a long-standing policy of pricing products responsibly. For the period 1994 through 2004 in the United States, the weighted average compound annual growth rate of Johnson & Johnson price increases for health care products (prescription and over-the-counter drugs, hospital and professional products) was below the U.S. Consumer Price Index (CPI). Inflation rates, even though moderate in many parts of the world during 2004, continue to have an effect on worldwide economies and, consequently, on the way companies operate. In the face of increasing costs, the Company strives to maintain its profit margins through cost reduction programs, productivity improvements and periodic price increases. The Company faces various worldwide health care changes that may result in pricing pressures that include health care cost containment and government legislation relating to sales, promotions and reimbursement. The Company also operates in an environment increasingly hostile to intellectual property rights. Generic drug firms have filed Abbreviated New Drug Applications seeking to market generic forms of most of the Company's key pharmaceutical products, prior to expiration of the applicable patents covering those products. In the event the Company is not successful in defending a lawsuit resulting from an Abbreviated New Drug Application filing, the generic firms will then introduce generic versions of the product at issue, resulting in very substantial market share and revenue losses. For further information see the discussion on "Litigation Against Filers of Abbreviated New Drug Applications" in Note 12 to the unaudited interim consolidated financial statements. 39 CAUTIONARY FACTORS THAT MAY AFFECT FUTURE RESULTS This Form 10-Q contains forward-looking statements. Forward- looking statements do not relate strictly to historical or current facts and anticipate results based on management's plans that are subject to uncertainty. Forward-looking statements may be identified by the use of words like "plans," "expects," "will," "anticipates," "estimates" and other words of similar meaning in conjunction with, among other things, discussions of future operations, financial performance, the Company's strategy for growth, product development, regulatory approval, market position and expenditures. Forward-looking statements are based on current expectations of future events. The Company cannot guarantee that any forward- looking statement will be accurate, although the Company believes that it has been reasonable in its expectations and assumptions. Investors should realize that if underlying assumptions prove inaccurate or that unknown risks or uncertainties materialize, actual results could vary materially from the Company's expectations and projections. Investors are therefore cautioned not to place undue reliance on any forward-looking statements. The Company assumes no obligation to update any forward-looking statements as a result of new information or future events or developments. Risks and uncertainties include general industry conditions and competition; economic conditions, such as interest rate and currency exchange rate fluctuations; technological advances, new products and patents attained by competitors; challenges inherent in new product development, including obtaining regulatory approvals; challenges to patents; U.S. and foreign health care reforms and governmental laws and regulations; trends toward health care cost containment; increased scrutiny of the health care industry by government agencies; product efficacy or safety concerns resulting in product recalls or regulatory action. The Company's Annual Report on Form 10-K for the fiscal year ended January 2, 2005 contains, as an Exhibit, a discussion of additional factors that could cause actual results to differ from expectations. The Company notes these factors as permitted by the Private Securities Litigation Reform Act of 1995. Item 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK There has been no material change in the Company's assessment of its sensitivity to market risk since its presentation set forth in Item 7A, "Quantitative and Qualitative Disclosures About Market Risk," in its Annual Report on Form 10-K for the fiscal year ended January 2, 2005. Item 4 - CONTROLS AND PROCEDURES-EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES Disclosure controls and procedures. As of the end of the period covered by this report, management evaluated the effectiveness of 40 the Company's disclosure controls and procedures. The Company's disclosure controls and procedures are designed to ensure that the Company records, processes, summarizes and reports in a timely manner the information the Company is required to disclose in its reports filed under the Securities Exchange Act. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. William C. Weldon, Chairman and Chief Executive Officer, and Robert J. Darretta, Vice Chairman and Chief Financial Officer, reviewed and participated in this evaluation. Based on this evaluation, Messrs. Weldon and Darretta concluded that, as of the date of their evaluation, the Company's disclosure controls and procedures were effective. Internal control. During the period covered by this report, there were no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. Part II - Other Information Item 1 - Legal Proceedings The information called for by this item is incorporated herein by reference to Note 12 included in Part I, Notes to Consolidated Financial Statements. Item 2 - Unregistered Sales of Equity Securities and Use of Proceeds (c) Purchases of Equity Securities by the Issuer and Affiliated Purchasers. The following table provides information with respect to Common Stock purchases by the Company

during the fiscal second quarter of 2005. Common Stock purchases on the open market are made as part of a systematic plan to meet the Company's compensation programs. Fiscal Month Total Number of Average Price Paid Shares Purchased Per Share April 4 - May 1, 2005 2,386,000 $68.51 May 2 - May 29, 2005 785,300 $67.75 May 30 - July 3, 2005 1,780,400 $65.86 Item 4 - Submission of Matters to a Vote of Security Holders (a) The annual meeting of the shareholders of the Company was held on April 28, 2005. (b) Election of the directors is set forth in (c) below. 41 (c) The shareholders elected all the Company's nominees for director and ratified the appointment of PricewaterhouseCoopers LLP as the Company's independent auditors for the fiscal year 2005. The shareholders also approved of the 2005 Long-Term Incentive Plan. 1. Election of Directors: Shares For Shares Withheld M. S. Coleman 2,562,818,361 31,562,661 J. G. Cullen 2,564,660,453 29,720,569 R. J. Darretta 2,468,716,847 125,664,175 M. M. E. Johns 2,566,448,108 27,932,914 A. D. Jordan 2,535,248,036 59,132,986 A. G. Langbo 2,537,950,461 56,430,561 S. L. Lindquist 2,565,402,713 28,978,309 L. F. Mullin 2,562,474,674 31,906,348 C. A. Poon 2,532,852,391 61,528,631 S. S Reinemund 2,566,276,547 28,104,475 D. Satcher 2,564,456,446 29,924,576 W. C. Weldon 2,533,669,335 60,711,687 Abstain 26,983,548 Broker Non-vote - 2. Approval for Appointment of PricewaterhouseCoopers LLP: For 2,532,548,257 Against 39,560,123 Abstain 22,272,642 Broker Non-vote - 3. Approval for the 2005 Long-Term Incentive Plan. For 1,730,947,712 Against 343,780,724 Abstain 29,924,967 Broker Non-vote 489,727,619 Item 6 - Exhibits Exhibit 10.1 Form of Stock Option Certificate and Restricted Shares to Non-Employee Directors Certificate under the Johnson & Johnson 2005 Long-Term Incentive Plan - Filed with this document.* Exhibit 31.1 Certifications under Rule 13a- 14(a) of the Securities Exchange Act pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - Filed with this document. Exhibit 32.1 Certifications pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 - Furnished with this document. *Management contract or compensatory plan. 42 SIGNATURES Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. JOHNSON & JOHNSON (Registrant) Date: August 10, 2005 By /s/ R. J. DARRETTA R. J. DARRETTA Vice Chairman, Board of Directors; Chief Financial Officer and Director (Principal Financial Officer) Date: August 10, 2005 By /s/ S. J. COSGROVE S. J. COSGROVE Controller (Principal Accounting Officer) 43