

Annual Report 2006

A human race



GlaxoSmithKline

Do more, feel better, live longer

Financial summary

Results

	2006 £m	2005 £m	Sterling % growth	2006	2005	CER% growth* 2004	2003	2002
Turnover	23,225	21,660	7	9	7	1	5	7
Research and development	3,457	3,136						
Operating profit	7,808	6,874	14	17	16	–	8	13
Profit before taxation	7,799	6,732						
Profit after taxation for the year	5,498	4,816						
Profit attributable to shareholders	5,389	4,689						
	2006 pence	2005 pence						
Earnings per share	95.5p	82.6p	16	19	18	2	10	13
Diluted earnings per share	94.5p	82.0p						
	2006	2005		2006	2005	2004	2003	2002
Dividends per share	48p	44p		48p	44p	42p	41p	40p

Cash flow

	2006 £m	2005 £m
Net cash inflow from operating activities	4,357	5,958
Capital expenditure	1,590	1,181
Free cash flow	2,623	4,664
Dividends to shareholders	2,598	2,390
Purchase of GSK shares	1,348	999
Net debt	2,450	1,237

Share price

	2006	2005
Share price at 31st December	£13.44	£14.69

*CER% growth is on an IFRS basis for 2006 and 2005 and a UK GAAP, business performance basis for 2004 and earlier. In order to illustrate underlying performance, it is the Group's practice to discuss its results in terms of constant exchange rate (CER) growth. This represents growth calculated as if the exchange rates used to determine the results of overseas companies in Sterling had remained unchanged from those used in the previous year. CER% represents growth at constant exchange rates. Sterling% or £% represents growth at actual exchange rates.

Website

GlaxoSmithKline's website www.gsk.com gives additional information on the Group. Information made available on the website does not constitute part of this Annual Report.

Notice regarding limitations on Director liability under English Law

Under the UK Companies Act 2006, a new safe harbour limits the liability of Directors in respect of statements in and omissions from the Report of the Directors contained on pages 2 and 3 and 6 to 82, under English law the Directors would be liable to the company (but not to any third party) if the Report of the Directors contains errors as a result of recklessness or knowing misstatement or dishonest concealment of a material fact, but would not otherwise be liable.

Report of the Directors

Pages 2 and 3 and 6 to 82 inclusive consist of a Report of the Directors that has been drawn up and presented in accordance with and in reliance upon English company law and the liabilities of the Directors in connection with that report shall be subject to the limitations and restrictions provided by such law.

Cautionary statement regarding forward-looking statements

The Group's reports filed with or furnished to the US Securities and Exchange Commission (SEC), including this document and written information released, or oral statements made, to the public in the future by or on behalf of the Group, may contain forward-looking statements. Forward-looking statements give the Group's current expectations or forecasts of future events. An investor can identify these statements by the fact that they do not relate strictly to historical or current facts. They use words such as 'anticipate', 'estimate', 'expect', 'intend', 'will', 'project', 'plan', 'believe' and other words and terms of similar meaning in connection with any discussion of future operating or financial performance. In particular, these include statements relating to future actions, prospective products or product approvals, future performance or results of current and anticipated products, sales efforts, expenses, the outcome of contingencies such as legal proceedings, and financial results. The Group undertakes no obligation to update any forward-looking statements, whether as a result of new information, future events or otherwise.

Forward-looking statements involve inherent risks and uncertainties. The Group cautions investors that a number of important factors, including those in this document, could cause actual results to differ materially from those contained in any forward-looking statement. Such factors include, but are not limited to, those discussed under 'Risk factors' on pages 44 to 47 of this Annual Report.

Chairman's and CEO's summary

Every day we are involved in a race that unites more than 100,000 people at GSK: in finding new medicines and vaccines that meet unmet medical needs; in ensuring that patients have access to these new medicines regardless of their financial circumstances; and in meeting the expectations of our many stakeholders, including you – our shareholder. It is a race with many stages and we won't win them all. But, as we take part, we never forget the real focus of our efforts: **the human race.**

2006 was a year of positive achievement for GSK as we continued to make progress on all fronts. Sales growth is coming from an ever-widening portfolio of fast-growing products that, combined with good cost control, has enabled us to deliver a strong financial performance. We also have very healthy momentum in our pipeline, with ten new products added to our late-stage development efforts in the last 12 months. For all these reasons, we look to the future with confidence.

Financial performance and outlook

Your company delivered a strong financial performance in 2006. Turnover of £23.2 billion is an increase of 9 per cent at constant exchange rates (CER)*. Earnings per share (EPS) were 95.5 pence, with growth of 19 per cent.

This performance was driven by sales of key pharmaceutical products including *Seretide/Advair* for asthma and chronic obstructive pulmonary disease (COPD), the *Avandia* group of products for diabetes, *Coreg* for heart disease, *Lamictal* for epilepsy and bipolar disorder, *Valtrex* for herpes, and our vaccines.

Although we performed well in a tough environment, the US political climate together with investor concern over pipeline delays resulted in our share price ending the year 9 per cent lower than at 1st January 2006.

Looking ahead, we expect new clinical data to help deliver growth from *Seretide/Advair* and the *Avandia* group of products, and continued good performance from our vaccines business. We plan to launch new products in both our Pharmaceutical and Consumer Healthcare businesses. In addition, we expect to continue to achieve savings through improved operational efficiency. The combination of new products and enhanced efficiency will help offset the impact of generic competition to *Zofran* and *Wellbutrin XL* during the coming 12 months and we expect to deliver 2007 EPS growth of 8 to 10 per cent in CER terms.

Delivering our pipeline for patients

Our pipeline is significant, with 158 projects in clinical development at the end of February 2007.

Although we had some setbacks during the year, including cancellation of *Redona* for diabetes, we have a great ability to reload our pipeline. And it is beginning to flow strongly, delivering much-needed new treatments for patients and opportunities for us. We now have 31 major product opportunities in phase III development or registration and we plan to launch five major new pharmaceutical products in 2007: *Tykerb* for breast cancer, *Cervarix* to prevent cervical cancer, *Allermist/Avamys* for allergic rhinitis, *Coreg CR* for heart conditions and *Trexima* for migraine.

Our Consumer Healthcare portfolio will also be strengthened in 2007 with the launch of ten products, including *alli*, the first FDA-approved OTC treatment for weight loss in the USA.

Best place to work

We work hard to create a working environment where the best people can do their best work and the results of our biennial employee opinion survey demonstrated that we are enjoying real success. For overall satisfaction, GSK scored higher than any of our peers in the benchmark group of major companies and 90 per cent of managers are proud to work for GSK.

Playing our part

In 2006, our global community investment contributions were valued at £302 million, equivalent to 3.9 per cent of Group profit before tax. This is a significant sum, but such commitment is no less than should be expected from a company in our industry. We have the capability and the desire to reach out to patients and to find solutions to healthcare challenges worldwide, helping people do more, feel better and live longer.

A human race

For all our investment in technology, it is our people that make GSK so different. We could not succeed without their commitment, expertise and passion, and we thank them all for their outstanding efforts in 2006.

We also thank you, our shareholders, for your continued support during the year, together with our suppliers and business partners who work so hard on our behalf.

Our management team has again performed very well. In the past 12 months we welcomed to the Board Dr Moncef Slaoui, our new Chairman of R&D, on 17th May 2006, Dr Daniel Podolsky on 1st July 2006 and Dr Stephanie Burns on 12th February 2007. In addition to Moncef, the corporate executive team saw two changes. Jennie Younger left in June 2006 and was succeeded by Duncan Learmouth as Senior Vice President, Corporate Communications and Community Partnerships. Ford Calhoun retired in January 2007 and was succeeded by Bill Louv as Chief Information Officer. Our best wishes go to both Jennie and Ford and we thank them for the valuable skills, great contribution and good humour they brought to their roles over the years.



Sir Christopher Gent
Chairman



JP Garnier
Chief Executive Officer

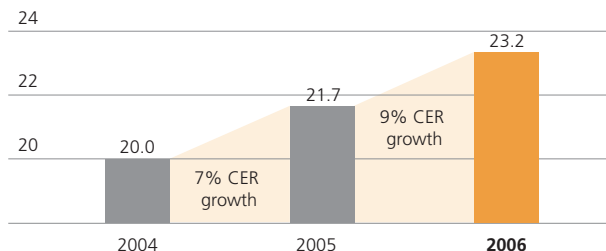
2006 performance overview

Key performance indicators

Turnover, earnings per share growth and total shareholder return

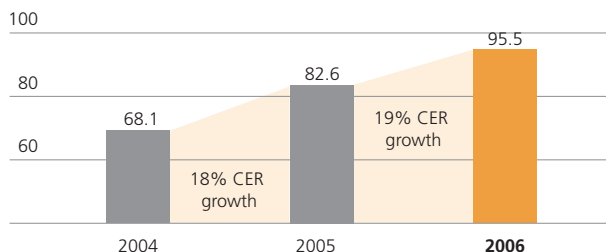
Turnover

£bn

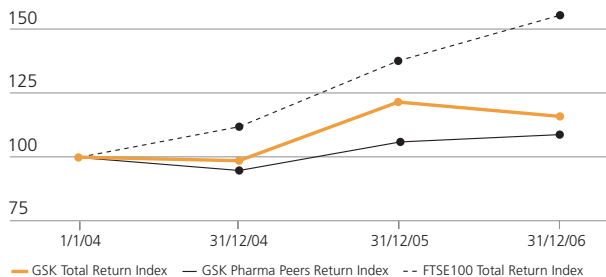


Earnings per share

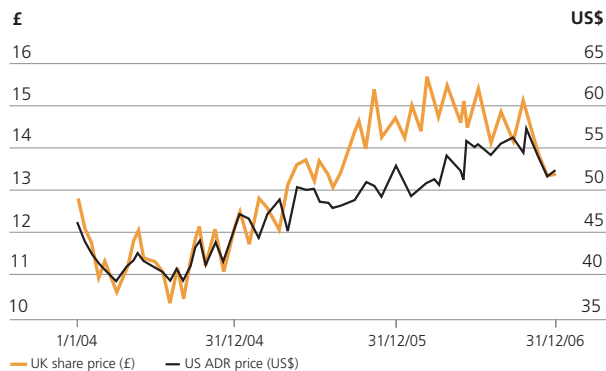
Pence



Total shareholder return



Share price



At 23rd February 2007, the share price was £14.50/\$56.92 per ADR

GSK's performance and development are driven by a number of important strategies

Strategies

Optimising the performance of key products

Both the Pharmaceutical and Consumer Healthcare businesses focus on ways to improve the return from the Group's intellectual property by maximising sales of key products.

GSK's activities include:

- achieving worldwide sales force excellence
- achieving Pharmaceutical and Consumer Healthcare marketing excellence
- maintaining the highest ethical standards
- improving the cost-effectiveness of operations

Delivering the product pipeline for patients

GSK aims to create the best product pipeline in the industry for the benefit of society. This includes developing a focused strategy to support the pipeline and manage the full life cycle of compounds from launch as prescription medicines through to potentially becoming over-the-counter products.

GSK measures R&D productivity by the number and level of innovation of the products it creates, and by the ability to address unmet patient needs.

Being the best place for the best people to do their best work

GSK is committed to creating the best place for the best people to do their best work by:

- recruiting and developing the best people in the industry
- supporting a culture of high reward for high performance
- ensuring good communication and employee involvement
- maintaining a diverse and healthy workforce

Improving access to medicines

GSK is finding innovative ways to bring medicines, vaccines and health education to patients in all countries, including those suffering from epidemics and neglected diseases.

Key developments in 2006

- Total turnover grew 9% to £23.2 billion – Pharmaceuticals up 9% to £20.1 billion; Consumer Healthcare up 6% to £3.1 billion
- Top ten Pharmaceutical products:
 - *Seretide/Advair* £3,313 million, up 11%
 - Vaccines products £1,692 million, up 23%
 - *Avandia* group of products £1,645 million, up 25%
 - *Lamictal* £996 million, up 19%
 - *Wellbutrin* £900 million, up 24%
 - *Zofran* £847 million, up 3%
 - *Valtrex* £845 million, up 24%
 - *Coreg* £779 million, up 38%
 - *Imigran/Imitrex* £711 million, up 3%
 - *Flixotide/Flovent* £659 million, up 5%
- High potential products *Avodart*, *Requip* and *Boniva* delivered combined sales of £579 million
- Top five Consumer Healthcare products:
 - *Lucozade* £301 million, up 14%
 - *Aquafresh* £283 million, down 3%
 - *Sensodyne* £257 million, up 19%
 - *Panadol* £207 million, up 6%
 - *Ribena* £169 million, down 1%
- Operating margin increased by 1.9 percentage points to 33.6% of turnover
- Continuing financial strength enabled the 2006 dividend to be increased to 48 pence (2005 – 44 pence)
- A new share buy-back programme of £6 billion over three years was announced

More details on page 31.

- In February 2007, GSK had 158 pharmaceutical and vaccine projects in clinical development, compared with 149 in February 2006
- 31 major product opportunities were in phase III development or registration (13 NCEs, 6 new vaccines, 12 PLEs), including:
 - *Cervarix* (cervical cancer)
 - *Tykerb* (breast cancer)
 - *Allermist* (allergic rhinitis)
 - *Coreg CR* (cardiovascular conditions)
 - *Trexima* (migraine)
 - H5N1 (pandemic 'flu vaccine)
- Late stage projects terminated included *Redona* for type 2 diabetes and brecanavir for HIV/AIDS

More details on page 12.

- The Group's biennial global leadership survey of over 10,000 managers in 2006 showed:
 - 91% (2004 – 91%) of managers believed "people in their department show commitment to performance with integrity"
 - 90% (2004 – 83%) of managers were "proud to be part of GlaxoSmithKline"
 - 86% (2004 – 77%) of managers would "gladly refer a friend or family member to work for GlaxoSmithKline"
- In 2006, 36.3% of the global management population was female (2005 – 35.5%)

More details on page 17.

- Global community investment was valued at £302 million, 3.9% of profit before tax
- The lymphatic filariasis elimination programme continued with another 155 million albendazole treatments donated, making almost 600 million treatments in total
- GSK shipped over 27 million *Combivir* tablets and nearly 59 million *Epivir* tablets to developing countries at not-for-profit prices. Approximately 120 million tablets were supplied by generic manufacturers licensed by GSK
- Other international humanitarian product donations totalled £22 million

More details on page 19.

History and development of the company

GlaxoSmithKline plc is a public limited company incorporated on 6th December 1999 under English law. Its shares are listed on the London Stock Exchange and the New York Stock Exchange. On 27th December 2000 the company acquired Glaxo Wellcome plc and SmithKline Beecham plc, both English public limited companies, by way of a scheme of arrangement for the merger of the two companies. Both Glaxo Wellcome and SmithKline Beecham were major global healthcare businesses.

GSK plc and its subsidiary and associated undertakings constitute a major global healthcare group engaged in the creation, discovery, development, manufacture and marketing of pharmaceutical and consumer health-related products.

GSK has its corporate head office in London. It also has operational headquarters in Philadelphia and Research Triangle Park, USA, and operations in some 117 countries, with products sold in over 140 countries. The principal research and development (R&D) facilities are in the UK, the USA, Japan, Italy, Spain and Belgium. Products are currently manufactured in some 37 countries.

The major markets for the Group's products are the USA, France, Japan, the UK, Italy, Germany and Spain.

Business segments

GSK operates principally in two industry segments:

- Pharmaceuticals (prescription pharmaceuticals and vaccines)
- Consumer Healthcare (over-the-counter medicines, oral care and nutritional healthcare).

Annual Report and Annual Review

This report is the Annual Report of GlaxoSmithKline plc for the year ended 31st December 2006, prepared in accordance with United Kingdom requirements. It was approved by the Board of Directors on 28th February 2007 and published on 2nd March 2007.

A summary report on the year, the Annual Review 2006, which is prepared in accordance with United Kingdom requirements and intended for the investor not needing the full detail of the Annual Report, is produced as a separate document. It includes the joint statement by the Chairman and the Chief Executive Officer, a summary review of operations, summary financial statements and a summary remuneration report. The Annual Review is issued to all shareholders. The Annual Report is issued to shareholders who have elected to receive it. Both documents are available on GlaxoSmithKline's corporate website at www.gsk.com.

In this Report 'GlaxoSmithKline', the 'Group' or 'GSK' means GlaxoSmithKline plc and its subsidiary undertakings; the 'company' means GlaxoSmithKline plc; 'GlaxoSmithKline share' means an Ordinary Share of GlaxoSmithKline plc of 25p; American Depositary Share (ADS) represents two GlaxoSmithKline shares.

Brand names appearing in italics throughout this report are trademarks either owned by and/or licensed to GlaxoSmithKline or associated companies, with the exception of *Baycol* and *Levitra*, trademarks of Bayer, *Boniva/Bonviva*, a trademark of Roche, *Citrucel*, a trademark of Merrell Pharmaceuticals, *Entereg*, a trademark of Adolor Corporation in the USA, *Hepsera*, a trademark of Gilead Sciences in some countries including the USA, *HuMax-CD20* a trademark of Genmab, *Integrilin*, a trademark of Millennium Pharmaceuticals, *Lymphostat B*, a trademark of Human Genome Sciences, *Nicoderm*, a trademark of Sanofi-Aventis, Pfizer Canada, Elan, Novartis, Merrell or GlaxoSmithKline, and *Vesicare*, a trademark of Astellas Pharmaceuticals in many countries and of Yamanouchi Pharmaceuticals in certain countries, all of which are used in certain countries under licence by the Group.

Mission

Our global quest is to improve the quality of human life by enabling people to do more, feel better and live longer.

Our Spirit

We undertake our quest with the enthusiasm of entrepreneurs, excited by the constant search for innovation. We value performance achieved with integrity. We will attain success as a world class global leader with each and every one of our people contributing with passion and an unmatched sense of urgency.

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Financial trends and ratios

	2006	Growth		2005	Growth		2004
	£m	CER%	£%	£m	CER%	£%	£m
Turnover – Pharmaceuticals	20,078	9	8	18,661	8	9	17,100
– Consumer Healthcare	3,147	6	5	2,999	2	4	2,886
Total	23,225	9	7	21,660	7	8	19,986
Cost of sales	(5,010)	6	5	(4,764)	8	9	(4,360)
Selling, general and administration	(7,257)	–	–	(7,250)	–	1	(7,201)
Research and development	(3,457)	11	10	(3,136)	8	8	(2,904)
Other operating income	307			364			235
Operating profit	7,808	17	14	6,874	16	19	5,756
Profit before taxation	7,799	19	16	6,732	13	16	5,779
Profit after taxation for the year	5,498	17	14	4,816	17	20	4,022
Profit attributable to minority interests	109			127			114
Profit attributable to shareholders	5,389			4,689			3,908
Earnings per share (pence)	95.5p	19	16	82.6p	18	21	68.1p
Diluted earnings per share (pence)	94.5p			82.0p			68.0p

Research and development

Pharmaceuticals	3,353			3,030			2,797
Consumer Healthcare	104			106			107
Total	3,457			3,136			2,904

Net finance cost cover

Net finance costs	65			194			186
Cover	121 times			36 times			32 times

Net finance cost cover is profit before tax plus net finance costs, divided by net finance costs.

Tax rate	29.5%			28.5%			30.4%
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Borrowings

Net debt	2,450			1,237			1,984
Gearing	25%			16%			33%

The gearing ratio is calculated as net debt as a percentage of total equity.

Exchange rates

The Group, as a multinational business, operates in many countries and earns revenues and incurs costs in many currencies. Its results are reported in Sterling and are affected by movements in exchange rates between Sterling and other currencies.

Average exchange rates prevailing during the period are used to translate the results and cash flows of overseas subsidiary and associated undertakings and joint ventures into Sterling. Period end rates are used to translate the net assets of those undertakings. The currencies which most influence these translations are the US dollar, the Euro and the Japanese Yen.

The business review discusses GSK's financial and non-financial activities, resources, developments and performance during 2006 and outlines the trends and factors which are likely to affect its future development under the following headings:

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The '2006 performance overview' on pages 2 and 3 form part of this business review.

Discussion of the Group's management structures and corporate governance procedures is set out in Corporate governance (pages 53 to 63).

The Remuneration Report gives details of the Group's policies on Directors' remuneration and the amounts earned by Directors and senior management in 2006 (pages 65 to 82).

The reconciliation to US accounting principles is set out in Note 41 to the financial statements.

Accounting presentation

This report is prepared under International Financial Reporting Standards (IFRS), as adopted by the European Union. GSK has taken advantage of an exemption which permits financial instruments to be accounted for and presented on a UK GAAP basis in 2004 and only in accordance with IAS 32 and IAS 39 from 1st January 2005.

Data for market share and market growth rates are GSK estimates based on the most recent data from independent external sources, and where appropriate, are valued in Sterling at relevant exchange rates. Figures quoted for product market share reflect sales by GSK and licensees.

The Group operates in many countries and earns revenues and incurs costs in many currencies. The results of the Group, as reported in Sterling, are affected by movements in exchange rates between Sterling and other currencies. Average exchange rates prevailing during the period are used to translate the results and cash flows of overseas subsidiary and associated undertakings and joint ventures into Sterling. Period end rates are used to translate the net assets of those undertakings. The currencies which most influence these translations are the US dollar, the Euro and the Japanese Yen.

In order to illustrate underlying performance, it is the Group's practice to discuss its results in terms of constant exchange rate (CER) growth. This represents growth calculated as if the exchange rates used to determine the results of overseas companies in Sterling had remained unchanged from those used in the previous year. CER% represents growth at constant exchange rates. £% represents growth at actual exchange rates.

Optimising the performance of key products

GSK undertakes a range of activities to maximise the commercial potential of its intellectual property by introducing innovative products, accelerating the process of bringing them to as many markets as possible, increasing brand recognition and improving access to new medicines. Both the pharmaceutical and consumer healthcare businesses focus on ways to optimise performance of key products through a number of initiatives. Some of these are:

Worldwide pharmaceutical sales force excellence

GSK's sales force has always ranked high in surveys with healthcare professionals. Worldwide Sales Force Excellence (WSFE) aims to improve customer satisfaction even further.

The time available for physicians to learn about new medicines and clinical studies is precious. Through the WSFE initiative, sales representatives strengthen product knowledge and learn to deliver patient-specific treatment options more efficiently and more effectively. Research shows that a sales visit is highly effective when a representative engages the physician in dialogue around patient types and supports the message with visual aids that illustrate clinical results.

A single global sales call model has been introduced that focuses on treating the patient through a dialogue about "when" a GSK medicine is appropriate, "why" it is effective and "how" to administer it safely. All field staff in GSK's key markets have been trained in this new approach. The entire sales organisation is involved in WSFE to bring about a cultural change that raises ethical standards and helps build long-term, trusting relationships with the healthcare community. In addition, a dashboard of key performance indicators, a product knowledge certification process and an effective leadership training programme have been established.

Superior product knowledge is essential in serving the needs of healthcare professionals. Physicians rely on GSK to keep them abreast of changes in prescribing information or new clinical studies involving GSK medicines. As a key goal of WSFE, GSK expanded its Annual Certification program to all countries. Over 30,000 representatives passed certification tests on the pathology, prescribing information and key messages of their leading products. Scores were consistently around 98%, with many representatives achieving a perfect score.

Pharmaceutical marketing excellence

Large numbers of patients suffering the effects of disease continue to be unable to benefit from innovative medicines and treatments. For example within Europe, around 50% of patients suffering from Chronic Obstructive Pulmonary Disease (COPD) are diagnosed and of those, only 60% receive regular maintenance drug therapy.

GSK's marketing initiative implements programmes to overcome the barriers to proper diagnosis and treatment, by providing accurate and balanced information on its products, to allow as many people as possible to benefit from GSK's medical advances. While these programmes are beginning to show effects, more needs to be done before the societal costs of disease will decrease.

Marketing codes

GSK is committed to ethical, responsible and patient-centred marketing. The Group's Pharmaceutical Marketing and Promotional Activity policy governs marketing activities and applies to all employees, suppliers, contractors and agents. This policy requires that all marketing and promotional activities are based on valid scientific evidence and comply with applicable laws and regulations.

This policy is supported by regional marketing practices codes in Europe, GSK's International region, Japan and the USA. These codes apply the same ethical standards but reflect differences in market structures, national healthcare systems and regulations. They incorporate the principles of industry codes of practice such as the European Federation of Pharmaceutical Industries Associations, the International Federation of Pharmaceutical Manufacturers Associations, Japan Pharmaceutical Manufacturers Association and Pharmaceutical Research and Manufacturers of America marketing codes.

Next Generation Now

In 2006, US Pharmaceutical businesses created and implemented the Next Generation Now operating model for advertising agencies. Design of this model, which aims to improve creativity and productivity and achieve significant cost savings, involved a number of key areas. As a result professional brand accounts were consolidated under a single agency, which increased access to the best talent, streamlined account management and reduced rates. The team also instituted key changes for agency reviews and created financial parameters and resource guides to improve decision making and processes.

Consumer Healthcare marketing excellence

The recent restructuring that placed greater emphasis on the brands' opportunities is now a major factor in the improved performance of this business. Through this restructuring, a team called the Future Group was created to drive the pipelines and marketing programmes for global brands with significant sales in multiple markets. For other large brands that have one dominant market, but may be available in several territories, a dedicated team drives each of these lead market brands for their dominant market. The remaining assets, termed enterprise brands, are locally managed by in-market commercial teams to retain their entrepreneurial spirit and relevance.

Delivering the product pipeline for patients

Research and Development – Pharmaceuticals

Since the merger, GSK R&D has developed one of the most robust pipelines of potential new medicines in the industry. In 2006 Pharmaceutical R&D was actively managing over 150 projects in human clinical trials across the globe. Delivering this pipeline to patients safely and efficiently is our number one goal.

Focus on the Patient

One objective unites the 15,500 people who work at GSK R&D, and that is staying focused on the patient. It drives them to discover potential treatments for disease and to develop innovative medicines that offer true benefit to patients. Reaching out to and speaking with patients and their families to understand the impact of disease on their lives, their work and their community are an essential part of this. GSK knows patients are waiting, and the focus on the patient is our driver to deliver the best every day.

Pharmaceutical R&D at GSK is organised around the discovery and development of medicines for patients. Discovery is conducted by Molecular Discovery Research and GSK's Centres of Excellence for Drug Discovery (CEDDs), and development by GSK's Medicine Development Centres (MDCs). Along the way, many other groups provide critical scientific input, conduct important experiments, and aid in managing the R&D process. These groups are described in more detail below.

Discovering potential medicines

Two components are needed in the discovery of new medicines – identification of the most important molecular targets that have potential to impact human disease and discovery of compounds that can modulate these targets to alleviate disease in an effective and safe way.

Molecular Discovery Research (MDR) produces the lead compounds that may interact with targets which form the basis of drug discovery efforts in GSK's CEDDs. In 2006, MDR progressed over 220 preclinical drug discovery programmes and in so doing performed hundreds of assays per week and provided the CEDDs with over 70 high-quality new lead compounds.

When GSK R&D designed the CEDDs, they integrated groups of scientists and clinicians and organised their work around specific disease areas. At no more than 300-400 people, each CEDD is nimble and entrepreneurial. GSK's nine therapeutically aligned CEDDs, based in Europe and the USA, are:

- Biopharmaceuticals – Stevenage, UK
- Cardiovascular – Upper Merion, USA
- Infectious Disease – Upper Merion and Research Triangle Park, USA
- Metabolic – Research Triangle Park, USA
- Oncology – Upper Providence, USA
- Macrolide Drug Discovery – Zagreb, Croatia (acquired Pliva Research Institute in May 2006)
- Neurology & Gastrointestinal Diseases – Harlow, UK
- Psychiatry – Verona, Italy
- Respiratory and Inflammation – Stevenage, UK.

Each CEDD is responsible for identifying the targets of most relevance in its therapeutic area and building on the lead compounds to produce a potential medicine. The fundamental steps in turning a lead compound into a medicine are optimising it for potency, efficacy and safety and defining the biology in animals and humans so that the medicine can be tested for effects in the right patient groups. These inventive steps are underpinned through scientific research and the application of informed judgement to develop creative solutions to the problems and challenges that inevitably arise in discovery and early development.

Once a candidate compound is selected, the CEDDs are responsible for undertaking the clinical studies necessary to demonstrate an effect sufficient to declare "proof of concept" – the first indication in patients that the new medicine works. Based on the profile of safety and efficacy a decision is then made on whether to progress the medicine into late-stage drug development, where large-scale clinical trials are conducted to confirm the efficacy and safety and gain regulatory approval to commercialise the product.

During the year, 19 new projects entered Phase II clinical trials for the first time.

GSK is committed to developing clinical science to ensure the understanding of disease processes in humans and learning as much as possible about the medicines in development. The application of experimental medicine is a major opportunity for the industry to optimise the drug discovery process. Advances in clinical imaging are revolutionising experimental medicine and opening opportunities to visualise the effects of medicines in humans. In 2006, GSK opened the Clinical Imaging Centre (CIC) on the biomedical research campus of Imperial College, London. The new £46 million facility is staffed by clinical investigation research groups working with state-of-the-art magnetic resonance imaging and positron emission tomography imaging systems. Facilities include radiochemistry, biology, image analysis and neurophysiology laboratories. The formidable capabilities of the CIC are augmented through multiple, global collaborations with academic imaging centres, established by GSK over the last decade.

In addition to the nine CEDDs, GSK also created a Centre of Excellence for External Drug Discovery (CEEDD) in 2005. This small team is responsible for delivering compounds to the proof of concept stage by establishing and managing long-term strategic collaborations with biotechnology companies, small and medium-sized pharmaceutical companies and academic institutions. In 2006, the CEEDD established four new collaborations and currently oversees a portfolio of 58 drug discovery projects ranging from target selection through to human clinical trials.

Developing medicines for patients

Preclinical Development (PCD) includes a wide range of activities throughout the entire medicines development process. In addition, this function is involved in the enhancement of existing products by devising more convenient formulations. Early in the development process, the metabolism and safety of compounds are evaluated in laboratory animals before testing in humans. The testing required in animals is highly regulated (see Animals and research, page 12).

PCD researchers investigate appropriate dosage forms (for example, tablets or inhalers) and develop formulations to enhance a drug's effectiveness and its ease of use by the patient.

Delivering the product pipeline for patients

continued

Processes and supporting analytical methods for drug synthesis and product formulation and delivery are scaled up to meet increasing supply requirements. This leads to the technical transfer of the processes and methods to manufacturing. The new product supply process, a partnership between R&D and Global Manufacturing and Supply, ensures that a robust product is developed for large-scale commercial manufacturing and launch.

In 2006, GSK redesigned the management of late-stage development by dividing the single large late-stage development organisation into three distinct, empowered entities. The first component, Medicines Development, is the collection of six therapeutically aligned Medicine Development Centres (MDCs). Each MDC has ultimate accountability for developing experimental drugs into regulatory-approved medicines for patients. The MDCs are responsible for creating value through the execution of full product development plans and ensuring strong partnerships with the rest of GSK, in particular the CEDDs and the other late-stage development groups.

The MDCs are based at the major USA and UK sites and are aligned with the following therapeutic areas:

- Cardiovascular/Metabolic
- Infectious Diseases including Diseases of the Developing World (DDW)
- Musculoskeletal/Inflammation/Gastrointestinal/Urology
- Neuroscience (Psychiatry/Neurology)
- Oncology
- Respiratory

The MDCs discharge their responsibilities through project teams for each medicine in development. These project teams are responsible for maximising the worldwide development opportunities for each product within their remit and to see that all the information needed to support the registration, safety programmes, pricing and formulary negotiations is available. Commercial input from Global Product Strategy and Commercial Operations ensures that regional marketing needs are integrated into development plans at an early stage.

The second component, Development Operations drives operational excellence in medicine delivery at the study, project and portfolio level. This is done by establishing integrated planning to ensure consistent and predictable drug project plans and supplying valued clinical development capabilities. In 2006, development operations managed clinical trials with over 30,000 active patients, handling everything from patient recruitment to data management to project planning. Development Operations is also responsible for helping to identify patients outside of traditional markets. In 2006, it identified more than 20,000 new patients, 39% of whom were outside of Western Europe and North America.

The Office of the Chief Medical Officer is the third component of late-stage development and is charged with the safety of patients involved in clinical trials, as well as the proper filing of the findings with regulatory authorities. All clinical trials sponsored by GSK, irrespective of where they take place, are conducted according to international standards of good clinical practice and applicable laws and regulations. The protocols are reviewed by the external regulatory agencies in the relevant countries where required and all protocols are considered by an ethics review committee, whose responsibilities cover the sites where the studies will take place.

Safety data are routinely collected throughout development programmes and are reported to national and regional regulatory agencies in line with applicable regulations.

GSK considers its Chief Medical Officer, working with the Global Safety Board, to be ultimately accountable for oversight of all major decisions regarding patient safety. The GSK Global Safety Board is responsible internally for approving pivotal studies and investigating any issues related to patient safety arising during the development programme. Information from GSK clinical trials is widely and easily available at the Clinical Trial Register on the website.

In 2006, GSK formed a dedicated pharmacogenetics group. GSK believes that pharmacogenetic research, correlating genetic data with response to medicine, will help its scientists understand how different people respond to the effects of a medicine, both those therapeutically intended and those causing adverse events. R&D is collecting DNA samples, under appropriate patient consent, in clinical studies to identify pharmacogenetic information which may help predict a patient's response. This information is intended to define patient groups likely to gain benefit from treatment or to suffer a side effect. Pharmacogenetics promises to provide physicians with information to help them select the medicine and dose most likely to benefit the patient and, in the long run, may help to reduce pipeline attrition and improve productivity.

In-licensing

GSK continues to identify compounds from other companies that would enhance the portfolio and to create innovative collaborations to ensure that the Group is regarded as the partner of choice for large and small companies.

The subjects of acquisitions, in-licensing, co-marketing/co-promotion, or future options arrangements in 2006 were:

- Genmab's *HuMax-CD20* (ofatumumab), anti CD20 Mab in oncology (Phase III) and rheumatoid arthritis (Phase II)
- HGS' *LymphoStat B* for lupus erythematosus (Phase III)
- Gilead/Myogen's ambrisentan (commercialisation, excluding USA), selective endothelin receptor antagonist for pulmonary arterial hypertension (Phase III), plus marketing and distribution agreement for GSK's *Folan* (in the USA) by Myogen
- Akros/Japan Tobacco's JTP-74057, a MEK inhibitor (preclinical)
- ChemoCentryx – options on preclinical assets and traficet (Phase II)
- EPIX – options on discovery targets and 5HT4 agonist (Phase I)
- Galapagos – options on discovery programmes in osteoarthritis (preclinical)
- Kissei's SGLT1 inhibitors for type 2 diabetes (preclinical)
- Pharmacoepia – options on discovery programmes (preclinical)
- Sirna's RNAi-based therapeutics for respiratory diseases (preclinical)
- Acquisition of the Pliva Research Institute

Extending the use of existing products

Once a product is launched, it is important to establish additional ways in which patients may be helped. This can be done through investigating whether other illnesses may be treated with the product or by the development of additional, more convenient dosage forms. Some developments reflect feedback from patients and medical professionals, while others are the result of continuing research into disease and its causes.

Delivering the product pipeline for patients

continued

In 2006, GSK received approval in the USA for a controlled-release version of *Coreg*, *Coreg CR*, which allows once-daily dosing for hypertension and mild to severe heart failure. The product will be launched in the USA in Q1 2007. GSK also began a novel investigation to determine whether its diabetes treatment, rosiglitazone XR is effective in Alzheimer's Disease. The scientific basis for this programme was developed thanks to the pharmacogenetics work undertaken with rosiglitazone over the past seven years.

Managing the portfolio

Key projects reaching significant milestones are reviewed each month by the Product Management Board (PMB), which is responsible for determining if a medicine has met criteria for passing into the next phase of development.

Progress of the portfolio is communicated to investors and the media at regular intervals during the year. Details of GSK's product development pipeline are given on pages 13 to 16.

Risk in R&D

Pharmaceutical R&D, by its very nature, is an inherently risky venture. From the time a potential medicine is discovered until it becomes an approved medicine can take 10-15 years. Further, only one in ten molecules that starts human clinical trials ever reaches regulatory approval. The nine out of ten that fail can be discontinued for a variety of reasons, from insufficient safety thresholds to lack of efficacy to manufacturing hurdles. These discontinuations occur despite extensive predictive testing. Late-stage projects terminated during 2006 included brecanavir for HIV and *Redona* for diabetes.

Research and development – vaccines

The majority of GSK's vaccine activities are conducted at its biologicals headquarters in Rixensart and Wavre, Belgium. These include research, clinical development, regulatory strategy, commercial strategy, scaling up, vaccine production, packaging and all other support functions. The discovery and development of a new vaccine is a complex process requiring long-term investment. In R&D over 1,500 scientists are devoted to developing new vaccines and more cost-effective and convenient combination vaccines to prevent infections that cause serious medical problems worldwide. GSK is also targeting therapeutic vaccines that may prevent relapse in cancer patients. Thanks to the use of innovative technologies and its global business model, GSK is a fast-growing vaccine maker, delivering value by contributing to the health and well-being of people, in every generation around the world.

Vaccine discovery involves many collaborations with academia and the biotech industry to identify new vaccine antigens which are then expressed in yeast, bacteria or mammalian cells and purified to a very high level.

This is followed by formulation of the clinical lots of the vaccine. This may involve mixing antigens with selected GSK novel proprietary adjuvant systems, which are designed to enhance the immune response. The first step is to evaluate the safety and efficacy of the candidate vaccine in a preclinical setting, usually involving an animal model. The candidate vaccine is then tested in clinical trials in healthy individuals to evaluate safety and effectiveness in inducing an immune response to protect the body from infection encountered later in a natural setting (Phase VI). Large-scale field trials in healthy individuals follow to establish safety and efficacy in a cross section of the population (Phase III).

The results obtained during clinical trials and data regarding the development of a quality and large-scale production process and facilities are then combined into a regulatory file which is submitted to the authorities in the countries where the vaccine will be made available.

After launch, post marketing studies of considerable size are set up to assess vaccination programmes and to monitor vaccine safety (Phase IV).

Vaccine manufacturing is particularly complex as it requires the use of innovative technologies and living micro-organisms. Sophisticated quality assurance and quality control procedures are in place to ensure both quality and safety of the vaccines and this commonly includes animal use according to health authorities' requirements. Due to their biological nature, individual health authorities may subject vaccines to a second control to guarantee the highest quality standards.

GSK has been increasing its capacity to supply vaccines across the globe by developing a unique global manufacturing network based on three major regional hubs in Europe, North America and Asia. After the establishment of its North American hub in 2005 through three major acquisitions, GSK further strengthened in 2006 its vaccine capabilities in both Asia and Europe:

- investing more than £100 million to set up a vaccine manufacturing site dedicated to the primary production of paediatric vaccines in Singapore
- opening in Gödöllő, Hungary, its €100 million primary production facility for the manufacturing of diphtheria, tetanus and pertussis antigens used in several paediatric combination vaccines
- investing more than €500 million in its vaccine manufacturing plant in St Amand-les-Eaux, France, to increase production capacity in formulation, filing, freeze-drying and packaging.

Diseases of the developing world

Continued investment in research into diseases that disproportionately affect the developing world is essential if there is to be a long-term improvement in the health of people who live in these regions. As part of GSK's response to this challenge, it operates a drug discovery unit, based at Tres Cantos (Spain), primarily dedicated to finding new medicines for malaria and tuberculosis. Additional research sites in the USA and the UK are focused on discovering new medicines to treat HIV/AIDS and drug resistant bacteria, while vaccine research is conducted in Rixensart (Belgium).

Medicines and vaccines that enter clinical trials are taken through development and regulatory processes by dedicated groups based in the UK, USA and Belgium. Through these R&D efforts, GSK is addressing the prevention and treatment of all three of the World Health Organization's (WHO) top priority diseases.

GSK currently has 14 clinical programmes of relevance to the developing world, 7 of which are aimed at producing vaccines and medicines for diseases that disproportionately affect developing countries.

Delivering the product pipeline for patients

continued

Public/Private Partnerships (PPPs) remain essential to fund research where there is no commercially viable market for a potential product. GSK is a leader in working in PPPs and continues to collaborate closely with many governments, academic centres, United Nations' agencies and other global funding bodies in this area, to maximise expertise and knowledge. This has the dual benefit of encouraging research and development and accelerating access to the medicines in the developing world.

Animals and research

For ethical, regulatory and scientific reasons, research using animals remains a small but vital part of research and development of new medicines and vaccines. GSK only uses animals where there is no alternative and only in the numbers required for each test. The Group strives to exceed regulatory standards in the care and use of the animals it uses and undergoes internal and external review to assure these standards.

The vast majority of the experimental methods do not use animals. GSK is actively engaged in research to develop and validate more tests that either avoid the use of animals in research or reduce the numbers needed. When animals are used in research unnecessary pain or suffering is scrupulously avoided.

GSK understands that use of animals for research purposes commands a high level of public interest. The GlaxoSmithKline Public Policy Position 'The care and ethical use of animals in research', and further information and reports, are available on the website, www.gsk.com or from Secretariat.

Research and development – Consumer Healthcare

The focus of R&D is to identify and develop novel products that benefit consumers in the over-the-counter (OTC), oral care and nutritional healthcare markets. To achieve a significant increase in innovation from internal and external sources, R&D has remodelled to deliver a more valuable pipeline of products. With this change, specific tasks that can be performed at lower cost outside the company have been transferred to external development partners. This transfer, along with other headcount reductions and savings, releases substantial funds for investment in additional innovation projects. The remodelling builds on the recently adopted Consumer Healthcare operating model whereby, for the Global brands, R&D mirrors the commercial structure, with brand-dedicated R&D teams paired with commercial brand teams and both located together at the Innovation Centres at Weybridge, UK or Parsippany, USA.

GSK's pipeline

At the end of February 2007, GSK had nearly 210 pharmaceutical and vaccine projects in development. Of these, 158 are in the clinic comprising 94 NCEs, 41 PLEs and 23 vaccines, compared with 118 in 2001.

In the last 12 months, 4 NCEs, 3 new vaccines and 3 in-licensed assets entered late-stage development.

GSK now has 31 major product opportunities in phase III development or registration, comprising 13 new chemical entities (NCEs), 6 new vaccines and 12 product line extensions (PLEs).

Major NCEs and vaccines in phase III development:

- ambriasantan – for hypertension
- *Lymphostat-B** – for lupus
- casopitant* – for post-operative and chemotherapy-induced vomiting and nausea
- pazopanib* – for prevention of tumour growth
- mepolizumab – for hypereosinophilic syndrome
- *Promacta** – for patients with low platelet count
- New generation 'flu vaccine*
- *Globorix* – a new combination paediatric vaccine against hepatitis B, diphtheria, meningitis A and C
- New meningitis vaccine against meningitis C and Y and Hib*
- *Synflorix* – vaccine to prevent pneumococcal disease.

(* entered late-stage in the last 12 months)

Major NCEs and vaccines filed:

- *Allermist/Avamys* – for hay fever; US approval expected in first half of 2007
- *Altanax/Altargo* – for skin infections; approval expected in 2007
- *Entereg* – for post-operative ileus, approval expected in 2007
- *Tykerb* – for breast cancer; US approval expected in first half of 2007
- *Cervarix* – vaccine to prevent cervical cancer; European and International launches expected in second half of 2007
- H5N1 pandemic vaccine.

Late-stage assets in-licensed during the last 12 months:

- *HuMax-CD20* – for the treatment of leukaemia and non-Hodgkin's lymphoma
- gepirone ER – for major depressive disorder
- XP13512 – for restless legs syndrome and treatment of neuropathic pain.

In 2007, GSK expects to launch 5 major new pharmaceutical products. For further details of these developments, and information on other important launches/filings expected in 2007, see GSK outlook on page 44.

This maturity in the late stage pipeline is expected to lead to an increase in registrations in the coming years. The content of the drug development portfolio will change over time as new compounds progress from discovery to development and from development to the market. Owing to the nature of the drug development process, many of these compounds, especially those in early stages of investigation, may be terminated as they progress through development. Phase I NCEs with multiple indications are counted only once. NCEs in later phases are counted by each indication. For competitive reasons, new projects in pre-clinical development have not been disclosed and some project types may not have been identified.

GSK's policy is to seek to obtain patent protection on all protectable inventions discovered or developed through its R&D activities. Patent protection for new active ingredients is available in all significant markets and protection can also be obtained, for example, on new pharmaceutical formulations, manufacturing processes, medical uses and special devices for administering products, see page 23.

Delivering the product pipeline for patients

continued

Key

†	In-license or other alliance relationship with third party	NDA	New drug application (USA)
S	Date of first submission	Phase I	Evaluation of clinical pharmacology, usually conducted in volunteers
A	Date of first regulatory approval (for MAA, this is the first EU approval letter)	Phase II	Determination of dose and initial evaluation of efficacy, conducted in a small number of patients
AL	Approvable letter indicates that ultimately approval can be given subject to resolution of outstanding queries	Phase III	Large comparative study (compound versus placebo and/or established treatment) in patients to establish clinical benefit and safety.
MAA	Marketing authorisation application (Europe)		

Estimated submission dates are only disclosed where they are within 12 months of the date of the chart. This date represents the most likely year of submission where it is considered that there is a reasonably high probability of successfully meeting the date assuming the clinical data meets the expected end-points of the clinical trials.

Compound/Product	Type	Indication	Phase	Estimated submission dates	
				MAA	NDA
Cardiovascular & Metabolic					
256073	high affinity nicotinic acid receptor (HM74A) agonist	dyslipidaemia	I		
568859 [†]	lipoprotein-associated phospholipase A2 (Lp-PLA2) inhibitor	atherosclerosis	I		
813893	factor Xa inhibitor	prevention of stroke in atrial fibrillation	I		
856553	p38 kinase inhibitor	atherosclerosis (also rheumatoid arthritis & chronic obstructive pulmonary disease, COPD)	I		
rilapladib [†]	Lp-PLA2 inhibitor	atherosclerosis	I		
501516 [†]	peroxisome proliferator-activator receptor (PPAR) delta agonist	dyslipidaemia	II		
681323	p38 kinase inhibitor	atherosclerosis (also COPD, neuropathic pain & rheumatoid arthritis)	II		
darapladib [†]	Lp-PLA2 inhibitor	atherosclerosis	II/III		
ambrisentan [†]	endothelin A antagonist	pulmonary arterial hypertension	III	2007	N/A
Coreg CR [†] + ACE inhibitor	beta blocker + angiotensin converting enzyme inhibitor	hypertension – fixed dose combination	III	N/A	
Arixtra	synthetic factor Xa inhibitor	treatment of acute coronary syndrome	Approvable	S:Jul06	AL:Feb07
Coreg CR [†]	beta blocker	hypertension & congestive heart failure – once-daily	Approved	N/A	A:Oct06
Metabolic projects					
189075 [†]	sodium dependent glucose transport (SGLT2) inhibitor	obesity	I		
376501	PPAR gamma partial agonist	type 2 diabetes	I		
625019	PPAR pan agonist	type 2 diabetes & metabolic syndrome	I		
189075 [†]	SGLT2 inhibitor	type 2 diabetes	II		
677954	PPAR pan agonist	type 2 diabetes, metabolic syndrome & dyslipidaemia	II		
869682 [†]	SGLT2 inhibitor	obesity	II		
albiglutide (716155) [†]	glucagon-like peptide 1 agonist	type 2 diabetes	II		
Avandia	PPAR gamma agonist	atherosclerosis in type 2 diabetes	II		
Avandamet XR	PPAR gamma agonist + metformin	type 2 diabetes – extended release	III	N/A	2007
Avandia	PPAR gamma agonist	prevention of diabetes	III	N/A	2007
Avandia	PPAR gamma agonist	prevention of disease progression	III	N/A	2007
Avandia + simvastatin	PPAR gamma agonist + statin	type 2 diabetes	III	N/A	2007
Avandaryl/Avaglim [†]	PPAR gamma agonist + sulphonylurea	type 2 diabetes – fixed dose combination	Approved	A:Jun06	A:Dec05
Infectious Diseases					
565154	oral pleuromutilin	treatment of bacterial infections	I		
742510	oral pleuromutilin	treatment of bacterial infections	I		
farglitazar	PPAR gamma agonist	hepatic fibrosis	II		
sitamaquine	8-aminoquinoline	treatment of visceral leishmaniasis	II		N/A
tafenoquine [†]	8-aminoquinoline	<i>Plasmodium vivax</i> malaria	II		
chlorproguanil, dapsone + artesunate (CDA) [†]	antifolate + artemisinin	treatment of uncomplicated malaria	III	2008	N/A
Altabax/Altargo	topical pleuromutilin	bacterial skin infections	Approvable	S:Jun06	AL:Dec06
Antivirals					
625433	polymerase inhibitor	hepatitis C	I		
825780 [†]	DNA antiviral vaccine	HIV infection	I		
364735 [†]	integrase inhibitor	HIV infection	II		
Relenza [†]	neuraminidase inhibitor	influenza prophylaxis	Approved	A:Aug06	A:Mar06

Delivering the product pipeline for patients

continued

Compound/Product	Type	Indication	Phase	Estimated submission dates	
				MAA	NDA
Musculoskeletal, Inflammation, Gastrointestinal & Urology					
221149	oxytocin antagonist	threatened pre-term labour	I		
232802	3G-selective oestrogen receptor modulator	treatment of menopausal symptoms	I		
267268	vitronectin integrin antagonist	age-related macular degeneration	I		
315234	monoclonal antibody	rheumatoid arthritis	I		
366074 [†]	potassium channel opener	overactive bladder	I		
751689 [†]	calcium antagonist	osteoporosis	I		
768974 [†]	parathyroid hormone agonist	osteoporosis	I		
relacatib [†]	cathepsin K inhibitor	osteoporosis & osteoarthritis (also bone metastases)	I		
274150	selective iNOS inhibitor	rheumatoid arthritis (also migraine)	II		
681323	p38 kinase inhibitor (oral)	rheumatoid arthritis (also atherosclerosis, COPD & neuropathic pain)	II		
856553	p38 kinase inhibitor (oral)	rheumatoid arthritis (also atherosclerosis & COPD)	II		
876008 [†]	corticotrophin releasing factor (CRF1) antagonist	irritable bowel syndrome (also depression & anxiety)	II		
casopitant	NK1 antagonist	overactive bladder (also depression & anxiety, chemotherapy induced & postoperative nausea & vomiting)	II		
dutasteride + testosterone	5-alpha reductase inhibitor + testosterone	hypogonadism – fixed dose combination	II		
<i>HuMax-CD20</i>	human monoclonal antibody	rheumatoid arthritis (chronic lymphocytic leukaemia & non-Hodgkin's lymphoma)	II		
(ofatumumab) [†]					
mepolizumab	anti-IL5 monoclonal antibody	eosinophilic esophagitis (also severe asthma & nasal polyposis)	II		
rosiglitazone XR	PPAR gamma agonist	rheumatoid arthritis (also Alzheimer's disease)	II		
solabegron	beta3 adrenergic agonist	irritable bowel syndrome	II		
solabegron	beta3 adrenergic agonist	overactive bladder	II		
<i>Avodart</i> + alpha blocker	5-alpha reductase inhibitor + alpha blocker	benign prostatic hyperplasia – fixed dose combination	III		
<i>Avodart</i>	5-alpha reductase inhibitor	reduction in the risk of prostate cancer	III		
belimumab [†]	anti-B lymphocyte stimulator monoclonal antibody	systemic lupus erythematosus	III		
<i>Entereg/Entrereg</i> [†]	peripheral mu-opioid antagonist	opioid induced bowel dysfunction	III		
mepolizumab	anti-IL5 monoclonal antibody	hypereosinophilic syndrome (also severe asthma & nasal polyposis)	III		
<i>Entereg/Entrereg</i> [†]	peripheral mu-opioid antagonist	post operative ileus	Approvable		AL:Jul05 & AL:Nov06
<i>Boniva/Bonviva</i> [†]	bisphosphonate	treatment of postmenopausal osteoporosis – i.v. injection	Approved	A:Mar06	A:Jan06
Neurosciences					
163090	5HT1 antagonist	depression & anxiety	I		
189254	histamine H3 antagonist	dementia	I		
239512	histamine H3 antagonist	dementia	I		
561679 [†]	CRF1 antagonist	depression & anxiety	I		
588045	5HT1 antagonist	depression & anxiety	I		
598809	dopamine D3 antagonist	drug dependency	I		
729327	AMPA receptor modulator	schizophrenia	I		
823296	NK1 antagonist	depression & anxiety	I		
274150	selective iNOS inhibitor	migraine (also rheumatoid arthritis)	II		
372475 [†]	triple (5HT/noradrenaline/dopamine) re-uptake inhibitor	depression	II		
468816	glycine antagonist	smoking cessation	II		
649868 [†]	orexin antagonist	sleep disorders	II		
681323	p38 kinase inhibitor	neuropathic pain (also atherosclerosis, COPD & rheumatoid arthritis)	II		
683699 [†]	dual alpha4 integrin antagonist (VLA4)	multiple sclerosis	II		
742457	5HT6 antagonist	dementia	II		
773812	mixed 5HT/dopaminergic antagonist	schizophrenia	II		
842166	non-cannabinoid CB2 agonist	inflammatory pain	II		
876008 [†]	CRF1 antagonist	depression & anxiety (also irritable bowel syndrome)	II		
casopitant	NK1 antagonist	depression & anxiety (also overactive bladder, chemotherapy induced & postoperative nausea & vomiting)	II		
talnetant	NK3 antagonist	schizophrenia	II		
gepirone ER [†]	5HT1a agonist	major depressive disorder, once-daily	III		2007
<i>Lamictal XR</i>	sodium channel inhibitor	epilepsy – partial generalised tonic-clonic seizures, once-daily	III	N/A	2007
rosiglitazone XR	PPAR gamma agonist	Alzheimer's disease (also rheumatoid arthritis)	III		
<i>Lamictal XR</i>	sodium channel inhibitor	epilepsy – partial seizures, once-daily	Submitted	N/A	S:Nov06
<i>Requip</i> extended release	non-ergot dopamine agonist	restless legs syndrome	Submitted	N/A	S:Oct06
<i>Requip Modutab/XL</i>	non-ergot dopamine agonist	Parkinson's disease – once-daily controlled release formulation	Submitted	S:Dec05	S:Feb07
24 hour [†]					
<i>Trexima</i> [†]	5HT1 agonist + naproxen	migraine – fixed dose combination	Approvable	N/A	AL:Jun06
<i>Wellbutrin XL</i> [†]	noradrenaline/dopamine re-uptake inhibitor	seasonal affective disorder	Approved	N/A	A:Jun06
<i>Wellbutrin XL/XR</i> [†]	noradrenaline/dopamine re-uptake inhibitor	depression	Approved	A:Dec06	A:Aug06

Delivering the product pipeline for patients

continued

Compound/Product	Type	Indication	Phase	Estimated submission dates	
				MAA	NDA
Oncology					
559448 [†]	thrombopoietin agonist	thrombocytopenia	I		
626616 [†]	human kinase inhibitor	chemoprotection	I		
pazopanib	vascular endothelial growth factor (VEGF) tyrosine kinase inhibitor	non-small cell lung cancer & colorectal cancer (in combination with other treatment regimens)	I		
relacatib [†]	cathepsin K inhibitor	bone metastases (also osteoporosis & osteoarthritis)	I		
pazopanib + <i>Tykerb</i>	VEGF tyrosine kinase inhibitor + ErbB-2 and epidermal growth factor receptor (EGFR) dual kinase inhibitor	breast cancer	II		
pazopanib + <i>Tykerb</i>	VEGF tyrosine kinase inhibitor + ErbB-2 and EGFR dual kinase inhibitor	other cancers	II		
<i>Promacta</i> (eltrombopag) [†]	thrombopoietin agonist	chemotherapy induced thrombocytopenia	II		
<i>Promacta</i> (eltrombopag) [†]	thrombopoietin agonist	hepatitis C	II		
casopitant	NK1 antagonist	chemotherapy induced & postoperative* nausea & vomiting (*USA only) (also overactive bladder, depression & anxiety)	III		
<i>HuMax-CD20</i> (ofatumumab) [†]	human monoclonal antibody	chronic lymphocytic leukaemia & non-Hodgkin's lymphoma (also rheumatoid arthritis)	III		
<i>Hycamtin</i>	topo-isomerase I inhibitor	ovarian cancer first-line therapy	III		
<i>Hycamtin</i>	topo-isomerase I inhibitor	small cell lung cancer second-line therapy – oral formulation	III	2007	2007
pazopanib	VEGF tyrosine kinase inhibitor	renal cell cancer	III		
<i>Promacta</i> (eltrombopag) [†]	thrombopoietin agonist	long-term idiopathic thrombocytopenic purpura	III		
<i>Promacta</i> (eltrombopag) [†]	thrombopoietin agonist	short-term idiopathic thrombocytopenic purpura	III		2007/08
<i>Tykerb</i>	ErbB-2 and EGFR dual kinase inhibitor	breast cancer, adjuvant therapy	III		
<i>Tykerb</i>	ErbB-2 and EGFR dual kinase inhibitor	breast cancer, first-line therapy	III		
<i>Tykerb</i>	ErbB-2 and EGFR dual kinase inhibitor	head & neck squamous cell carcinomas	III		
<i>Tykerb</i>	ErbB-2 and EGFR dual kinase inhibitor	refractory breast cancer	Submitted	S:Oct06	S:Sep06
<i>Arranon/Atricane</i>	guanine arabinoside prodrug	acute lymphoblastic leukaemia & lymphomas	Approved	S:May06	A:Oct05
<i>Hycamtin</i>	topo-isomerase I inhibitor	cervical cancer, second-line therapy	Approved	A:Nov06	A:Jun06
Respiratory					
256066	PDE IV inhibitor (inhaled)	COPD	I		
573719	muscarinic acetylcholine antagonist	COPD	I		
679586	monoclonal antibody	severe asthma	I		
961081 [†]	muscarinic antagonist, beta2 agonist	COPD	I		
159797 [†]	long-acting beta2 agonist	COPD, also COPD & asthma in combination with a glucocorticoid agonist	II		
159802 [†]	long-acting beta2 agonist	COPD, also COPD & asthma in combination with a glucocorticoid agonist	II		
233705	muscarinic acetylcholine antagonist	COPD	II		
256066	PDE IV inhibitor (inhaled)	asthma	II		
256066	PDE IV inhibitor (intranasal)	allergic rhinitis	II		
597901 [†]	long-acting beta2 agonist	COPD, also COPD & asthma in combination with a glucocorticoid agonist	II		
642444 [†]	long-acting beta2 agonist	COPD, also COPD & asthma in combination with a glucocorticoid agonist	II		
678007 [†]	long-acting beta2 agonist	COPD, also COPD & asthma in combination with a glucocorticoid agonist	II		
681323	p38 kinase inhibitor (oral)	COPD (also atherosclerosis, neuropathic pain & rheumatoid arthritis)	II		
685698	glucocorticoid agonist	asthma & COPD in combination with a long-acting beta2 agonist (also as <i>Avamys/Allermist</i> for allergic rhinitis)	II		
784568	glucocorticoid agonist (intranasal)	allergic rhinitis	II		
799943	glucocorticoid agonist	asthma & COPD in combination with a long-acting beta2 agonist	II		
856553	p38 kinase inhibitor (oral)	COPD (also atherosclerosis & rheumatoid arthritis)	II		
870086	novel glucocorticoid agonist	asthma	II		
mepolizumab	anti-IL5 monoclonal antibody	severe asthma & nasal polyposis (also hypereosinophilic syndrome & eosinophilic esophagitis)	II		
<i>Avamys/Allermist</i>	glucocorticoid agonist	allergic rhinitis	Submitted	S:Jul06	S:Jun06
<i>Seretide/Advair</i>	beta2 agonist/inhaled corticosteroid	COPD – mortality claim	Submitted	S:Sep06	S:Oct06
<i>Ariflo</i>	PDE IV inhibitor (oral)	COPD	Approvable		AL:Oct03
<i>Seretide</i>	beta2 agonist/inhaled corticosteroid	asthma – initial maintenance therapy	Approved	A:Jul06	N/A
<i>Seretide/Advair</i>	beta2 agonist/inhaled corticosteroid	asthma – non-CFC inhaler	Approved	A:Jun00	A:Jun06

Delivering the product pipeline for patients

continued

Compound/Product	Type	Indication	Phase	Estimated submission dates	
				MAA	NDA
Paediatric Vaccines					
MenACWY-TT	conjugated	<i>Neisseria meningitidis</i> groups A, C, W & Y disease prophylaxis	II		
Globorix	conjugated	diphtheria, tetanus, pertussis, hepatitis B, <i>Haemophilus influenzae</i> type b disease, <i>Neisseria meningitidis</i> groups A & C disease prophylaxis	III	2007	
Hib-MenCY-TT	conjugated	<i>Neisseria meningitidis</i> groups C & Y disease & <i>Haemophilus influenzae</i> type b disease prophylaxis	III		
Infanrix-IPV	subunit – inactivated	diphtheria, tetanus, pertussis + poliomyelitis prophylaxis (booster 5th dose)	III		2007
Synflorix	conjugated	<i>Streptococcus pneumoniae</i> disease and non-typeable <i>Haemophilus influenzae</i> prophylaxis for children	III	2007	
Priorix-Tetra	live attenuated	measles, mumps, rubella & varicella prophylaxis	Approved	A:Jul06	
Rotarix ¹	live attenuated – oral	rotavirus induced gastroenteritis prophylaxis	Approved	A:Feb06	2007
Other Vaccines					
HIV	recombinant	HIV infection prophylaxis	I		
<i>S. pneumoniae</i> elderly	recombinant – conjugated	<i>Streptococcus pneumoniae</i> disease prophylaxis	I		
Dengue fever	attenuated tetravalent vaccine	Dengue fever prophylaxis	II		
Epstein-Barr virus ¹	recombinant	EBV infection prophylaxis	II		
Hepatitis E virus ²	recombinant	hepatitis E prophylaxis	II		
Mosquirix	recombinant	malaria prophylaxis	II		
Tuberculosis	recombinant	tuberculosis prophylaxis	II		
Varicella Zoster virus	recombinant	Varicella Zoster prevention	II		
New generation 'flu vaccine	inactivated split-trivalent	seasonal influenza prophylaxis for the elderly	III		
Simplirix	recombinant	genital herpes prophylaxis	III		
Daronrix	inactivated whole-aluminium salt – monovalent	pandemic influenza prophylaxis	Submitted	S:Dec05	
'Flu pre-pandemic	H5N1 inactivated split- monovalent	pandemic influenza prophylaxis	Submitted	S:Jan07	
Cervarix ¹	recombinant	human papilloma virus infection prophylaxis	Submitted	S:Mar06	2007
FluLaval	inactivated split	influenza prophylaxis	Approved	2007	A:Oct06
Pharmaccines					
P501	recombinant	treatment of prostate cancer	I		
MAGE-A3	recombinant	treatment of non-small cell lung cancer & melanoma	II		

Being the best place for the best people to do their best work

GlaxoSmithKline people

GlaxoSmithKline is committed to creating the best place for the best people to do their best work to deliver the Group's business strategy. The Group employs over 100,000 people in more than 117 countries.

Recruitment, talent management and leadership development

Attracting the best people in the industry is critical to enhancing and sustaining GSK's performance. The Group's Talent Solutions recruiters in the USA and UK are focused on pro-active identification of talented external candidates for key jobs.

The annual performance and development planning (PDP) process ensures that employees set business aligned objectives and behavioural goals. PDPs are reviewed throughout the year, culminating with an end of year review that is factored into compensation decisions.

The annual talent management cycle identifies the highest performing people in each business and function and key talent is developed through tailored management and leadership programmes (for more detail see the Group's Corporate Responsibility Report), exposure to top management through programmes such as the Chief Executive Forum and stretch assignments. A pool of potential successors is identified for each Vice-President position and other critical roles in the organisation.

Performance and reward

Reward systems are designed to support a culture of high performance and to attract and retain the best people. Performance based pay and bonuses, share awards and share options align employee interests with the meeting of business targets.

Communication and employee involvement

The Group conducts a Global Leadership Survey (GLS) every two years. The most recent survey was conducted in 2006 among more than 10,000 managers to gauge opinions on critical issues such as culture and confidence in the Group's future. Scores on morale and engagement have steadily increased since 2002 and compare very favourably with global benchmarks (42 top-ranked companies). In the 2006 survey, 90% of managers were "proud to be part of GlaxoSmithKline" and 86% would "gladly refer a friend or family member to work for GlaxoSmithKline". Each business and function develops action plans to address areas for improvement based on results from the GLS and other surveys.

The Group also consults employees on changes that affect them and discusses developments in the businesses with a European Employee Consultation Forum and similar bodies in countries where this is national practice. In 2006 in the UK, a new national consultation forum was created. The UK Information and Consultation Forum is made up of 15 elected employee representatives and seven management representatives. It meets regularly so that employee views can be taken into account before major changes affecting all employees are implemented.

Business ethics and reputation

Performance with integrity is central to operating at GSK. The 2006 GLS showed 91% believe that "people in their department show commitment to performance with integrity" and 82% agree that they "can report unethical practices without fear of reprisal".

To engage a wider range of managers, the half-day workshop on Ethical Decision-making (attended by 479 leaders in 2005) has been extended to three e-learning modules, which are being implemented across the businesses. So far, over 400 people have completed at least one of the three modules.

Maintaining Standards

GSK expects employees to meet high ethical standards in all aspects of business by conducting activities with honesty and integrity, adhering to corporate responsibility principles and complying with applicable laws and regulations. GSK audits its operations to ensure relevant standards expected, such as those in marketing practices, are reached or exceeded.

Commitment to the GSK Code of Conduct is reinforced each year by a senior management certification programme, and in 2006 over 12,000 managers certified they had complied with "Performance with Integrity" principles.

The PDP process includes an assessment of how well employees have implemented the GSK Spirit, the principles used to define GSK's culture. This may have a significant impact on bonus payments and may also affect future career development. In this way the Group holds employees accountable for delivering performance with high standards of integrity to protect and enhance GSK's reputation.

Diversity

The diversity and inclusion initiatives focus on improving performance by responding to the diverse needs of employees, customers and external stakeholders. In the fifth year of the annual Multicultural Marketing and Diversity Awards, 14 teams from around the world highlighted innovative activities that demonstrated business impact. In 2006, the global management population was 63.7% male and 36.3% female. For more details on diversity measures, see the Employment Practices section of the Corporate Responsibility report.

The Group is committed to employment policies free from discrimination against existing or potential staff on the grounds of age, race, ethnic and national origin, gender, sexual orientation, faith or disability. GSK is committed to offering people with disabilities access to the full range of recruitment and career opportunities. Every effort is made to retain and support employees who become disabled while working with the Group.

Health and well-being

Healthy employees and healthy ways of working contribute to the sustained performance of the Group. Global policies on employee health are supported by mandatory standards that integrate employee health and safety and environmental requirements. These standards are applied to all the Group's facilities and operations worldwide.

A commitment to flexible working through flexi-time, teleconferencing, remote working and flexible work schedules, recognises that employees work best in an environment that helps them integrate their work and personal lives.

During 2006, the Group's Employee Health Management function developed a resilience programme which has now been translated into 11 languages and adopted in 12 countries.

Improving access to medicines

Access to healthcare in the developing world

Access to healthcare in developing countries remains a major challenge to the global community. The problem, which is rooted in poverty, demands a significant mobilisation of political will, additional resources and a true spirit of partnership. GSK continues to play a vital role, through its commitment to R&D into diseases particularly prevalent in the developing world, through its programme of preferential pricing for its anti-retrovirals (ARVs), anti-malarials and vaccines, through its community investment programmes (see page 19) and through its willingness to seek innovative solutions, such as voluntary licencing arrangements.

Preferential pricing programme

GSK has offered its vaccines to key organisations for vaccination programmes in developing countries at preferential prices for over 20 years. The Group also sets a single not-for-profit price for each of its ARVs and anti-malarials to a wide range of customers in the Least Developed Countries (UN definition) and sub-Saharan Africa, as well as Country Coordinating Mechanism-projects fully funded by the Global Fund to Fight AIDS, TB, and Malaria and the US President's Emergency Plan for AIDS Relief (PEPFAR). In July 2006, GSK introduced two new ARVs, *Kivexa* and *Telzir*, to its not-for-profit offering and reduced prices to GSK's abacavir-containing products by up to 30%.

GSK is committed to contributing to health improvements in a sustainable manner. The prices for its ARVs and anti-malarials are therefore set at levels at which no profit is made, but direct costs are covered, allowing supply to be sustained for as long as required. During 2006, GSK shipped to developing countries over 27 million tablets of not-for-profit-priced *Combivir* and nearly 59 million tablets of not-for-profit-priced *Epivir*. Some of our licensees are now supplying key markets in a more significant way.

The offer of not-for-profit prices requires a sustainable framework, combining GSK's commitment to preferential pricing with commitments from governments of the developed world to avoid price referencing against preferentially priced medicines and from all governments to help prevent product diversion. GSK has taken steps to minimise the threat of diversion with the registration of specific access packs or access tablets (differentiated red tablet as opposed to the traditional white) for its key ARVs. GSK is the only company to have registered its ARVs under the European Union's Anti-Diversion Regulation.

Innovative solutions

GSK has shown industry leadership in granting voluntary licences to eight generic companies for the manufacture and supply of ARVs to both the public and private sectors in sub-Saharan Africa. GSK is also a leader in collaborating in Public-Private Partnerships to enable new drug discovery and development to take place more effectively.

Looking ahead

GSK will continue to build on its product, pricing and partnership commitments to help improve healthcare in the developing world. However, a significant increase in funding from the global community is still needed. It is also important to maintain incentives for R&D through protection of intellectual property.

While much has been achieved, sustainable progress will only occur if the significant barriers that stand in the way of better access to healthcare are tackled as a shared responsibility by all sectors of global society – governments, international agencies, charities, academic institutions, the pharmaceutical industry and others.

Access to medicines in the developed world

Programmes in the USA

GSK is working to provide meaningful access to medicines for people with limited financial resources and without prescription drug insurance. In 2006, GSK's US patient assistance programmes provided \$370 million worth of medicines, valued at wholesale acquisition cost, to 402,000 qualifying low income US residents.

GSK has worked to expand its patient assistance programme and created "GSK Access" to include those enrolled in Medicare Part D. Beginning in 2007, GSK Access will help eligible Part-D-enrolled patients who have spent at least \$600 of their own money during the current year on outpatient medicines and may qualify to receive GSK medicines free.

For uninsured Americans who do not qualify for Medicare or Medicaid, GSK and 11 other pharmaceutical companies created Together Rx Access, a programme for qualified individuals offering reductions in the pharmacy cost on more than 300 medicines. Over 820,000 Together Rx Access cardholders, saved about \$24 million in 2006.

GSK participates in the Partnership for Prescription Assistance (PPA), the largest national programme dedicated to helping people in need access prescription medicines. PPA has helped more than 3 million US patients in need find programmes providing significant help. GSK and other US pharmaceutical companies launched the programme in 2005 working with healthcare, physician and patient advocacy organisations.

Patient Advocacy

The Patient Advocacy initiative has demonstrated significant progress since its inception in 2002. Initially launched as a US programme, it is now a critical initiative throughout GSK. Patient Advocacy teams in the USA and Europe share best practices and established processes to optimise interaction with patient groups. Typically these relationships provide mutual opportunities: to learn about patient needs and priorities and for patient groups to develop an understanding of drug development challenges.

In 2006, Patient Advocacy Leaders Summits were held in the USA, Brazil and Japan, with over 1,000 attending GSK sponsored meetings. In the USA, GSK partnered with the Centers for Medicaid and Medicare Services to develop 12 regional meetings to educate patient groups on the new Medicare Drug Benefit and increase programme participation.

Programmes in other countries

The Group has also introduced Orange Cards providing discounts on certain GSK prescription medicines for eligible patients in Bulgaria, Lithuania and Ukraine. The nature of the discounts varies between countries and the way in which the healthcare system operates.

In September 2006, GSK announced an agreement with the Russian Government to supply anti-retroviral medicines, for the treatment of HIV/AIDS, at discounted prices. The agreement is the first direct, federal purchase of anti-retroviral medicines in Russia.

Preparing for a 'flu pandemic

As part of its commitment to support governments and health authorities to prepare for the threat of an influenza pandemic, GSK announced in 2006 promising data on the immunogenicity of its new generation H5N1 pandemic influenza vaccine. This innovative pandemic vaccine candidate is also believed to have the potential to offer protection against drifted variants of the H5N1 virus allowing a proactive pre-pandemic vaccination approach to be considered.

Corporate responsibility and community investment

Commitment to corporate responsibility

GSK is committed to connecting business decisions to ethical, social and environmental concerns. Thus, corporate responsibility is an integral and embedded part of the way GSK does business.

In 2003, GSK published a set of Corporate Responsibility principles to provide guidance on the standards to which the Group is committed. This sets out the approach to 10 areas: standards of ethical conduct, research and innovation, products and customers, access to medicines, employment practices, human rights, community investment, caring for the environment, leadership and advocacy, and engagement with stakeholders. The Group reports annually on progress in upholding these principles in its Corporate Responsibility Report, which is available on the website at www.gsk.com.

Partnership success

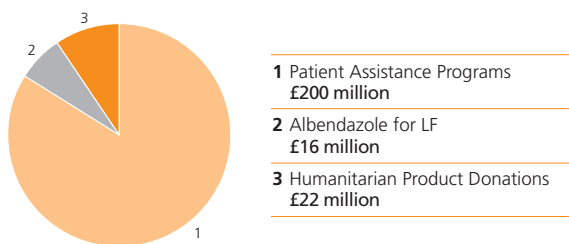
GSK works as a partner with under-served communities in the developed and developing world. It supports programmes that are innovative and sustainable and that bring real benefits to these communities. The Group engages with numerous external stakeholders, funds community-led initiatives around the world and donates medicines to support humanitarian efforts and community-based healthcare.

Community investment

GSK's global community investment activities in 2006 were valued at £302 million, equivalent to 3.9% of Group profit before tax. This comprised product donations of £238 million, cash giving of £46 million, other in-kind donations of £3 million and costs of £15 million to manage and deliver community programmes in 109 countries.

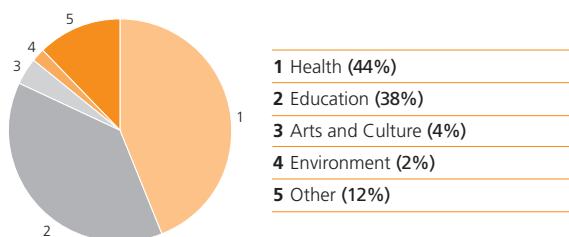
Product donations and cash giving in 2006 were as follows:

1. Product donations



GSK's cash giving was targeted primarily at health and education initiatives.

2. Breakdown of cash giving



In the UK, GSK contributed £7 million in 2006 to its continuing programme of charitable activities supporting over 100 organisations in health, medical research, science education, the arts and the environment.

Programmes in North America focused on improving public education and access to better healthcare for children and seniors both nationally and locally with funding of \$34 million.

GSK does not operate a single charitable foundation for its community investment programmes, but has a number of country based foundations. The grants made by these foundations in 2006 are included in the investment total.

Global Health Programmes

Eliminating lymphatic filariasis

The Group's effort to eliminate the disabling disease, lymphatic filariasis (LF) from the world, continued in close partnership with the governments of countries where the disease is endemic, the WHO and over 40 partner organisations. GSK is committed to donate as much of the anti-parasitic drug albendazole as required to treat the one billion people at risk in 80 countries. In 2006, 155 million albendazole treatments, worth £16 million at wholesale acquisition cost, were donated to 34 countries. Since the global elimination programme started in 2000, a cumulative total of almost 600 million albendazole treatments have been donated.

Positive Action on HIV/AIDS

Positive Action is GSK's pioneering global programme working with communities affected by AIDS. Started in 1992, it supports community-based organisations to deliver effective HIV and AIDS education, prevention and healthcare services. During 2006, Positive Action worked with 26 partners to support programmes in 17 countries. Positive Action was the principal sponsor of the community section (The Global Village) at the International AIDS Conference held in Toronto.

The GlaxoSmithKline African Malaria Partnership

Since 2002, this partnership has supported three behavioural development programmes working in eight African countries. The programmes have targeted nearly two million people, focusing particularly on young children and pregnant women, encouraging effective prevention measures, prompt treatment and antenatal malaria management. In addition, GSK's malaria advocacy programme 'Mobilising for Malaria' launched country Coalitions Against Malaria in the UK, Belgium, France, Ethiopia and Cameroon to increase awareness of malaria and mobilise resources.

Corporate responsibility and community investment

continued

PHASE

The PHASE programme (Personal Hygiene And Sanitation Education), initiated by GSK in 1998, is now providing education to thousands of school children in Kenya, Uganda, Zambia, Nicaragua, Peru and Bangladesh to improve their health and hygiene to fight infectious diseases. In 2006 the Group committed three year funding of \$0.9 million to extend the programme to Mexico and Tajikistan in partnership with Save the Children, USA.

Humanitarian product donations

During 2006, GSK donated essential products, such as antibiotics, through non-profit partners including AmeriCares, MAP International and Project HOPE, to support humanitarian relief efforts and community healthcare. The total value of the Group's international humanitarian product donations was £22 million. This excludes albendazole donated as part of the Group's commitment to the lymphatic filariasis elimination programme. Product donations are valued at wholesale acquisition cost, which is the wholesale list price, not including discounts, and is a standard industry method.

Community initiatives

GSK is dedicated to strengthening the fabric of communities through providing health and education initiatives and support for local civic and cultural institutions that improve the quality of life.

GSK's contribution to improve healthcare includes a grant of almost \$3 million over three years to the Children's Health Fund to expand their Referral Management Initiative (RMI) to sites in Philadelphia, including the Delaware Valley Community Health Center. The RMI ensures continuity of specialist medical care for high-risk children who are often homeless.

The annual GlaxoSmithKline IMPACT Awards recognise excellence in the work of non-profit community health organisations across the UK and in the Greater Philadelphia area of the USA. Over 20 charities receive unrestricted awards for their work dealing with diverse and difficult social issues such as domestic violence, sexual health services for young people, community health support and counselling services.

To further medical research, over £592,000 was provided to four UK medical charities, Asthma UK, the British Retinitis Pigmentosa Society, Deafness Research UK and the Muscular Dystrophy Campaign.

Education initiatives

GSK's efforts to improve public and science education included a \$1 million endowment to the National Board for Professional Teaching Standards to increase the number of science teachers attaining certification initially in the North Carolina and Philadelphia areas, but extending to all 50 states.

During 2006, GSK supported the Institute for a Competitive Workforce, a new business coalition staffed by the Business Civic Leadership Center of the US Chamber of Commerce. This is aimed at improving education and creating a skilled workforce.

GSK also supports a range of local initiatives in the USA. For example 'Science in the Summer', a free library-based science education programme in the Philadelphia area teaching basic scientific concepts, continued to receive support with a grant of almost \$400,000.

In 2006, GSK helped to launch PUPPETS: Talking Science, Engaging Science into UK primary schools, with grants of over £480,000 over four years. The puppets and their supporting materials increase children's engagement and motivate them to talk about science. GSK's support will enable 9,000 teachers to attend subsidised training over the next four years, and provide a set of puppets and training materials to each of the participating schools.

Only 25% of secondary school science teachers in England are chemistry specialists. Chemistry for Non-Specialists has been developed by the Royal Society of Chemistry to train teachers to teach chemistry with confidence, flair and enthusiasm. GSK is supporting the programme with a donation of £450,000 over three years starting in 2006.

Employee involvement

GSK employees are encouraged to contribute to their local communities through employee volunteering schemes. Support varies around the world, but includes employee time, cash donations to charities where employees volunteer and a matching gifts programme.

In 2006 in the USA, the Group matched more than 17,500 employee and retiree gifts at a value of over \$5 million. The Group also matched more than \$1.3 million of employee donations to GSK's annual United Way campaign. GSK's GIVE program provided grants of almost \$340,000 to more than 365 organisations where US employees have volunteered.

GSK's Making a Difference programme in the UK provided grants of £225,000 to over 380 non-profit organisations and registered charities based on employee involvement.

Global manufacturing and supply

GSK manufactures a large portfolio of products, ranging from tablets and toothpaste to inhalers and complex capsules, in over 28,000 different pack sizes and presentations.

Manufacture of medicines starts with the development of a therapeutic active ingredient (bulk active) in a selected formulation. Global Manufacturing and Supply (GMS) develops manufacturing processes for full scale volume production of active compounds at primary manufacturing sites. Secondary sites then convert these active compounds into finished medicines.

Each year GMS produces around 6,000 tonnes of bulk actives and more than four billion packs, which are sold in over 140 countries. It also supports about 2,000 new product and line extension launches every year.

By adopting leading edge practices and developing its people, GMS provides:

- a secure source of supply of high quality products
- compliance with regulatory requirements and customer expectations
- best in class cost.

Organisation

GMS operates as a single global network of 80 sites in 37 countries. The sites are grouped into four supply divisions, based on common business drivers, areas of expertise and the commercial activities that they support.

Primary supply

Primary supply has 12 sites in six countries, supplying high quality, competitively priced bulk actives. The division is focused on improvements in primary technologies and processes.

New product and global supply

There are 10 new product and global supply sites in seven countries. Sites work closely with R&D's development team to ensure that the right technical competencies are in place to support rapid and successful new product introduction. These sites also ensure secure supply of key brands that are sold across many markets. This division is the focal point for developing and introducing new secondary manufacturing technologies for GMS.

Regional pharma supply

Regional pharma supply operates to supply key products in particular regions or markets and tailor packaging to meet specific local requirements. This division focuses on reducing costs, allowing GSK to compete more effectively in all its markets. There are 29 regional pharma supply sites in 22 countries.

Consumer Healthcare supply

Consumer Healthcare supply delivers high-quality, competitively priced products and supports rapid new product introduction in a highly innovative and competitive business with far shorter time frames than pharmaceuticals. New technologies have become a fundamental platform for driving innovation, lowering costs and providing flexibility in operations. There are 29 sites in 21 countries in Consumer Healthcare supply.

Operational excellence

Within GMS, Operational Excellence provides the capability to drive improvements in process robustness, quality, performance and customer service. Operational Excellence is underpinned by extensive education and a culture of continuous improvement.

Vision Factory

GSK introduced the Vision Factory initiative to work towards a simpler, more efficient operating model within GMS. Vision Factory is enabling manufacturing operations to accelerate the improvement in performance and cost control.

Quality

The quality organisation oversees product quality across the supply chain, from suppliers and third party manufacturers through manufacturing to the supply operations that deliver products into the market. The quality organisation focuses on improving quality and compliance by increasing product quality understanding, and harmonising the quality approach across all sites. GSK continues to work with the FDA on Good Manufacturing Practice for the 21st Century and other initiatives.

External suppliers

GMS spends over £2 billion annually with many external suppliers, purchasing active ingredients, chemical intermediates, packaging components, and part-finished and finished products. It takes appropriate steps to protect our supply chains from any disruption.

Procurement

Widely recognised by industry analysts as a best practice leader, procurement works collaboratively to develop and implement sourcing strategies which ensures that GSK receives best value when buying goods and services. GSK leverages its procurement activities across the Group structure.

Vaccines supply chain

GSK biologicals' manufacturing network is based on three major regional hubs in Europe, North America and Asia. In Europe, vaccine manufacturing is located primarily at Rixensart and Wavre in Belgium, with three other sites in France, Germany and Hungary. In North America, GSK established its vaccine production network in 2005 through three major acquisitions: US based Corixa Corporation, with a production site in Hamilton, Montana, which manufactures MPL, a key component of GSK's adjuvant systems, a vaccine production site in Marietta, Pennsylvania and ID Biomedical with 'flu vaccine manufacturing facilities in Laval and Quebec, Canada. In Asia, new vaccine production facilities are being built in India and Singapore. Managing the vaccine supply chain involves anticipating market needs and using a flexible approach to be able to meet fluctuations in demand. These are based on forecasts from the different markets and firm orders from health authorities for mass vaccination campaigns.

Bulk, filling and packaging are carefully balanced and stocking of vaccines helps manage short-term increases in demand. Such increases result from disease outbreaks or increased demand from the public owing to disease awareness campaigns.

Regulatory environment

Regulation – Pharmaceuticals

GSK operates within a highly regulated environment. Regional and country-specific laws and regulations define the data required to show safety and efficacy of pharmaceutical products, as well as govern testing, approval, manufacturing, labelling and marketing of drugs. These regulatory requirements are a major factor in determining whether a marketable product may be successfully developed and the amount of time and expense associated with this development.

In Europe, pharmaceutical firms and regulators are managing a transition following the implementation of new medicines legislation at the end of 2005. Significant changes are being implemented including approval procedures, post marketing requirements, manufacturing controls, labelling requirements, pharmacovigilance processes and an increased emphasis on transparency of regulatory processes.

The climate of change is set to continue, with the finalisation of a new Paediatric Regulation at the end of 2006. This Regulation is aimed at stimulating industry research into paediatric indications, via intellectual property incentives. Implementation activities will continue during 2007/08, and the new provisions will become operational in 2008.

The EU Commission is championing a 'Better Regulation' initiative to cut red tape and over-regulation of Industry. GSK is actively supporting this initiative and a similar one in the UK. For example in the UK, GSK has made 50 wide ranging better regulation proposals to the government, covering significant areas of interest to the Group. Many have been positively received and some are being considered for incorporation into new regulations.

In the USA, the safety of prescription drugs remains a primary focus of the FDA and congressional oversight committees are evaluating the ability and resourcing of the FDA to continue to provide this important role. New safety-related legislation has been proposed by Congress which may be enacted in 2007, with likely impact on the pharmaceutical industry. As in Europe, evaluation of benefit and risk continues to be an important consideration for approval of a new drug by the FDA.

The FDA is in the second year of its Critical Path Initiative to facilitate innovation in drug development. New tools and processes such as pharmacogenomics, surrogate markers of efficacy and manufacturing innovations are being pursued to enhance development of safe and effective drugs. The pharmaceutical industry, including GSK, is collaborating with the FDA and National Institutes of Health in a number of these areas, including evaluation of new biomarkers.

The US government is making information about the benefits and risks of prescription drugs more readily available via the Internet, including the full prescribing information which is posted within one day of approval. GSK is now providing product labelling to the FDA in an electronic format which allows easier access to the key details in the prescribing information.

GSK is well placed to manage effectively these changes in the external regulatory environment.

Price controls

In many countries the prices of pharmaceutical products are controlled by law. Governments may also influence prices through their control of national healthcare organisations, which may bear a large part of the cost of supplying products to consumers.

Recent government healthcare reforms in countries such as France, Spain and Germany may restrict pricing and reimbursement.

In the USA, recent legislation on healthcare reform, cross-border trade, the acceleration of generics to market and increased patient contributions have further increased the focus on pricing. Currently, there are no government price controls over private sector purchases, but federal law requires pharmaceutical manufacturers to pay prescribed rebates on certain drugs in order to be eligible for reimbursement under Medicaid and other federal healthcare programmes.

Medicare

In 2006, the US Medicare program, a federally funded healthcare insurance program benefiting senior citizens and certain disabled Americans, included coverage for prescription medicines. This is a new benefit under the Medicare program and the most dramatic change in the program since its inception in the 1960s. The coverage is voluntary, includes brand-name and generic drugs and is open to the 41 million Americans with Medicare coverage.

A number of competing private organisations provide the new benefit with premiums subsidised by the government. Benefits must satisfy a minimum standard outlined in federal law. While the law provides incentives for manufacturers to negotiate prices with private plans, it does not provide for government price controls. The government provides additional help to more than 14 million people on Medicare with limited incomes and resources. Those qualifying beneficiaries pay no or reduced premiums and deductibles, and low copayments for their prescriptions.

Value for money

Payers around the world are concerned about the cost of healthcare and the pricing of medicines. The requirement to satisfy healthcare purchasers on value for money is becoming an additional hurdle for product acceptance over and above the regulatory tests of safety, efficacy and quality.

While it is appropriate for payers to seek value for money when purchasing medicines, this often translates into cost-containment measures that delay patient access to new medicines and make it difficult even for significantly improved therapies to achieve a price that reflects added value. Healthcare budgets could be managed in a more strategic and long-term manner. Focus should shift to value not cost and pricing should reflect value. Value should be defined broadly. What matters is whether a medicine works and responds to medical and patient needs. If so, it should be rewarded appropriately.

Regulatory environment

continued

Payers must also allocate their resources efficiently to provide the best health outcomes. Attention should be focused in three areas: prevention, innovation and better management of chronic diseases. As part of this triple solution, innovative medicines and vaccines will play a key role by preventing, or providing better treatments for expensive diseases such as cervical cancer, breast cancer, asthma, Alzheimer's and diabetes.

It is not possible to predict whether and to what extent, the Group's business will be affected by future legislative and regulatory developments relating to specific pharmaceutical products or their price.

Regulation – Consumer Healthcare

The consumer healthcare industry is subject to national regulation for the testing, approval, manufacturing, labelling and marketing of products. In many countries, high standards of technical appraisal involve a lengthy approval process before a new product is launched.

National regulatory authorisation is also required to approve the switch of products from prescription to OTC. The requirements include long-term experience of the quality, safety and efficacy of the product in a wide patient population and data to confirm that the relevant condition is both self-limiting and easily diagnosed by the consumer.

Intellectual property

Intellectual property is a key business asset for GSK. The effective legal protection of intellectual property is critical in ensuring a reasonable return on investment in R&D. Intellectual property can be protected by patents, trademarks, registered designs, copyrights and domain name registrations.

Certain markets, including the USA, the EU and Canada also provide a period of regulatory data exclusivity to qualifying drugs which are new chemical entities or which are new formulations or uses of marketed drugs. Manufacturers of generic drugs may, following any period of data exclusivity, launch, or attempt to launch, generic versions of patented drugs prior to normal patent expiry, arguing that the relevant patents are invalid and/or are not infringed by their product. Significant litigation concerning these challenges is summarised in Note 43 to the financial statements, 'Legal proceedings'.

Patents

GSK's policy is to seek to obtain patent protection on all protectable inventions discovered or developed through its R&D activities. Patent protection for new active ingredients is available in most significant markets, and protection can also be obtained for example for new pharmaceutical formulations, manufacturing processes, medical uses and special devices for administering products. Patents protecting new active ingredients are generally applied for early in the development process. Since the term of a patent in most countries is a set period from the filing date, typically 20 years, the effective term depends on how long a product is in development before launch. This leads to a variation in patent term on a product by product basis, although in a number of markets, including the USA and Europe, it is possible in certain circumstances to obtain a partial restoration of patent term to compensate for the length of the development process.

The patent position with respect to the active ingredients in significant products is as follows:

Avandia and *Avandamet*. The patent on rosiglitazone is not due to expire until 2012^{a,c} (USA) and 2013^b (Europe). Patents on the commercial form of the active ingredient rosiglitazone maleate are not due to expire until 2015 (USA) and 2014^b (Europe). Litigation challenging the validity of the patents protecting these products is ongoing in the USA^e.

Avodart. The patent on dutasteride is not due to expire until 2015^a (USA) and 2017^b (Europe).

Boniva. The patent on ibandronate is not due to expire until 2012^{a,b} (USA and Europe).

Combivir. The patent on the specific combination of lamivudine and zidovudine is not due to expire until 2012 (USA) and 2013^b (Europe).

Coreg. GSK is the exclusive licensee under the US patent on carvedilol, which is due to expire in 2007^{a,c}.

Epivir. The patent on lamivudine is not due to expire until 2010^{a,c} (USA) and 2011^b (Europe).

Imigran/Imitrex. The patent on sumatriptan is not due to expire until 2009^c (USA) and has expired in Europe (except Cyprus (2007), Italy and Switzerland (2008)). Litigation challenging the validity of the patent protecting this product in the USA has been settled^e.

Lamictal. The patent on lamotrigine is not due to expire until 2009^{a,c} (USA). Litigation challenging the validity of this patent in the USA has been settled. In Europe, the corresponding patent has expired and generic competition exists.

Levitra^d. GSK has co-promotion rights under the US patent on vardenafil, which is not due to expire until 2018.

Lexiva/Telzir. GSK is the exclusive licensee under the patent on fosamprenavir, which is not due to expire until 2017 (USA) and 2019^b (Europe).

Paxil/Seroxat. The patent on the commercial form of paroxetine expired in 2006 in Europe and is due to expire in 2007^c in the USA. Litigation relating to the validity and infringement of a patent directed to a method of manufacture of paroxetine hydrochloride anhydrate is ongoing in the USA^e. Generic competition on *Paxil* instant release (*IR*) and oral suspension has commenced in the USA, Europe and certain other markets. *Paxil CR* is protected by a formulation patent that is not due to expire until 2012. A generic manufacturer has applied for FDA approval of a generic form of *Paxil CR* asserting non-infringement of this patent^e.

Requip. The patent on ropinirole is not due to expire until 2007^a (USA) and 2008^b (Europe). A patent relating to the use of ropinirole in Parkinson's disease is not due to expire until 2008 (USA) and 2011^b (Europe). Litigation challenging the validity of the Parkinson's use patent is ongoing in the USA^e.

Seretide/Advair. The patent on the specific combination of salmeterol xinafoate and fluticasone propionate is not due to expire until 2010 (USA) and 2013^b (Europe). An application for re-issue of the US patent has been allowed by the US Patent and Trademark Office (USPTO)^e. The UK patent has been revoked by the UK courts. Patents on the individual ingredients have expired in the UK. In the USA, the patent on salmeterol xinafoate does not expire until 2008.

Regulatory environment

continued

Serevent. The patent on salmeterol xinafoate is not due to expire until 2008 in the USA. In Europe, the patent has expired, except France (2008^b) and Italy (2009^b).

Trizivir. The patent on the method of treatment using a combination of lamivudine, zidovudine and abacavir does not expire until 2016 (USA) and 2016 (Europe).

Valtrex. The patent on valaciclovir is not due to expire until 2009^a (USA) and 2009^b (Europe, except Greece and Spain 2008). Litigation challenging the validity of the patent in the USA^e is ongoing.

Wellbutrin SR, *Wellbutrin XL* and *Zyban*. The patent on the active ingredient has expired. There is now generic competition for the sustained release (*SR*) and instant release (*IR*) forms in the USA, and generic competition for the 300mg dosage form of *Wellbutrin XL* commenced in the USA in December 2006. In Europe, regulatory data exclusivity provides protection until 2009 in some markets. Litigation is ongoing in the USA relating to formulation patents covering *Wellbutrin XL* that expire in 2018^e.

Ziagen. The patent on abacavir is not due to expire until 2012^{a,c} (USA) and 2014^b (Europe).

Zofran. The patent on ondansetron has expired in the USA and Europe, (except France (2007^b) and Italy (2008^b)). A patent on use in treating emesis expired in 2006. In the USA, generic entry of ondansetron injection and oral solution dosage forms commenced in November 2006 and on tablet and orally disintegrating tablet dosage forms in December 2006. Generic competition has also now commenced in a number of countries in Europe.

- a) Including granted or pending patent term restoration under the Hatch-Waxman Act
- b) Including granted or pending extension of term by national or European supplementary protection certificates
- c) Including granted or pending extension of term for paediatric exclusivity
- d) A registered trademark of Bayer AG
- e) See Note 43 to financial statements 'Legal proceedings'

Trademarks

All of GSK's pharmaceutical products are protected by registered trademarks in major markets. There may be local variations, for example, in the USA the trademark *Paxil* is used instead of *Seroxat* and *Advair* is used instead of *Seretide*.

Trademark protection may generally be extended for as long as the trademark is used by renewing it when necessary. GSK's trademarks on pharmaceutical products are important for maintaining the brand identity of the product upon expiration of the patent.

The Consumer Healthcare trademarks are particularly important, as the business is very brand orientated and many products do not have patent protection.

Responsibility for environment, health and safety

Environment, health and safety (EHS) is a key element of corporate responsibility for the Group and has a high priority. Responsibility for EHS is at the highest level. There is a corporate group reporting to the General Counsel that has overall responsibility for providing governance and leadership on EHS issues. The head of this group makes regular reports to the Corporate Executive Team (CET) and the Audit and Corporate Responsibility Committees of the Board. Within the businesses operations managers are responsible for EHS and are supported by site-based EHS and occupational health staff.

EHS strategy and plan

GSK has a strategic planning process for EHS that looks forward 10 years but is reviewed every year. The plan is aligned with the GSK business drivers and includes management objectives with performance measures and targets. In 2006, GSK's progress in the first five years of the EHS Plan for Excellence was evaluated and a 10 year plan extending to 2015 was developed.

The first five years had focused on establishing the fundamentals and preparing programmes that would contribute to the environmental sustainability of the business. Successes in 2006 included greater integration of EHS into the manufacturing planning process, introduction of EHS directors in manufacturing executive teams, establishment of new performance targets, establishment of new targets for audit scores, that will be the same for GSK's own manufacturing sites and contract manufacturers, publication of positions on pharmaceuticals in the environment, the selection of hazardous chemicals in manufacturing and energy conservation. The next phase of the plan strengthens the focus on operational efficiency and renews the commitment to stakeholder engagement. The three aspirations for 2006 to 2015 are embedding EHS in the business, environmental sustainability and open and transparent stakeholder relations.

Strategic focus in 2006

The plan provides an area of special focus each year. In 2006, the focus was on embedding EHS in the business, making EHS an integral part of GSK's business processes and continuous improvement culture with the participation of all employees. The goal is to develop a culture where every employee is mindful of the importance of safe working and protecting the environment. While this was the 2006 focus it will take more than one year to accomplish.

Regulatory environment

continued

Part of embedding EHS in GSK meant each business developed its own plan for moving EHS forward based on its own risks and opportunities. Some accomplishments against the objectives that contributed to the overall focus were:

- to reduce the need for respiratory protective equipment occupational hygiene monitoring data were utilised to focus attention on the processes in most need of improvement
- to improve the efficiency of manufacturing processes it was agreed that all new products launched from 2006 to 2010 will be evaluated using green chemistry tools with a target to double the manufacturing efficiency, which will result in waste per tonne of product from new processes being reduced by half in comparison to existing processes
- to improve EHS management systems a target was set to improve audit scores and all pharmaceutical manufacturing sites will be required to be certified to ISO 14001 and OHSAS 18001 by 2010
- to minimise EHS risks arising from new product introduction and process changes EHS requirements and sustainability principles were incorporated into the product development process
- to improve EHS performance of R&D processes novel technologies will be explored.

EHS audits

As part of its governance responsibility, GSK conducts EHS audits of its sites, assessing performance against the EHS standards and assigning quantitative performance scores. In 2006, 32 sites were audited, 12 of these achieved audit scores of 80% or better. No site scored less than 50%. As part of the continuous improvement process, progress was monitored on actions arising from issues raised on all audits.

As part of the commitment to corporate responsibility and the proactive management of the GSK manufacturing and supply base, 36 suppliers were also assessed, representing about 10% of priority suppliers. This process evaluated the management of key EHS risks and impacts, as well as human rights issues, based on the Group's requirements for priority suppliers. Recommendations were made for improvements where needed.

EHS targets

As part of the EHS plan, targets are set every five years. 2006 was the baseline year for the next group of five-year targets. In the 2005 EHS report achievements against the targets for 2001-2005 were reported.

Progress towards meeting the targets for 2006-2010 will be tracked every year. Final data for 2006 will be published on the website www.gsk.com.

GSK selected its measures of performance improvement based on the potential for adverse impact on people or the environment, business continuity or business reputation. Most of the measures selected are similar to those reported by other companies and are recommended by the Global Reporting Initiative, a long-term, multi-stakeholder, international undertaking, to develop and disseminate globally applicable sustainability reporting guidelines. Targets have been set to eliminate CFCs from all uses by 2010 and each year to reduce energy use and non-hazardous waste disposed by 1%, reduce water use and Volatile organic compound (VOC) releases by 2% and reduce chemical oxygen demand of wastewater by 3%. All targets are normalised by sales.

EHS performance

The performance in 2006 was:

- CFC emissions from patient use of inhalers down 36% per £ sales
- volatile organic compound emissions down 22% per £ sales
- chemical oxygen demand in wastewater down 21% per £ sales
- non-hazardous waste disposed down 15% per £ sales
- energy use down 8% per £ sales
- water use down 5% per £ sales.

Sustainability

In the work towards sustainability, GSK is addressing the economic, environmental and social issues in research, manufacturing, sales and distribution of its medicines. Sustainability starts with healthcare solutions found by R&D and continues with sustainable solutions in manufacturing and sales. R&D is considering improving operational efficiency for new products. In the future, the EHS plan for excellence proposes investigating the use of renewable resources. The Group seeks dialogue with external stakeholders and considers their views when developing approaches to sustainable development. More information on EHS programmes and performance may be found on the GSK website.

World Market

World economy

The global economy remained relatively robust in 2006, with positive growth in many markets such as the USA and China. World Gross domestic product growth was estimated at 3.9%, up from 3.5% in 2005. Analysts expect it to fall back in 2007 and towards the end of 2006, the OECD trimmed its 2007 global growth forecast to 2.5%, the lowest rate since 2003.

Equity markets rose during 2006 and concerns regarding inflation started to recede as the year progressed only to return in some regions later in the year. Global oil prices hit \$78-a-barrel highs in mid-July following the crisis between Israel and Lebanon. As 2006 closed oil fell towards the \$60 mark, a level around which many analysts feel it will trade through 2007, barring unforeseen events.

In the USA, GDP growth slipped from a two year high of 5.5% in the first quarter of 2006 to 2.2% in the fourth quarter. This performance was impacted to a significant extent by a weakening housing market and a drop in new housing starts that is expected to continue throughout 2007. During 2006, US interest rates rose from 4.29% to 5.25%, the seventeenth rise in two and half years. In December, the US dollar fell to its lowest level for almost two years against the Euro and a 14-year low against Sterling. In 2007, the US economy is expected to experience a soft-landing rather than a major slowdown, with growth predicted to be in a range 2.5% to 3%.

After its rapid expansion in 2004 and 2005, the Chinese economy grew by over 10% in 2006, while India reported growth of 9.1%. India's Sensex Index gained 46% in value while Japan's Nikkei 225 Index moved ahead by 7% for the year. Japan is currently experiencing the longest period of uninterrupted growth since the Second World War, reporting GDP growth of 3.8% at the year-end.

Eurozone interest rates began the year at 2.25% before rising in five separate steps to 3.5% at the year end. Economic growth was 3.3% across the continent, up from 1.4% in 2005. Germany expanded by 3.7%, France by 2% and Spain by 4.0%. In the UK, interest rates rose to 5% in November, with the FTSE 100 gaining almost 11% in 2006. Economic growth was 2.7%, with the Treasury and the Bank of England expecting growth of more than 3% in 2007.

Exchange

The currencies that most influence the Group's results are the US dollar, the Euro and the Japanese Yen.

In 2006, the US dollar fell by 14% against the pound, to \$1.96 at the year-end. The year-end rates for the Euro weakened by 1% and the Japanese Yen by 15% against Sterling.

World market – pharmaceuticals

Global pharmaceutical sales increased by 8% in 2006 to £328 billion.

World market by geographic region	Value £bn	% of total	Growth £%
USA	145.0	44	9
Europe	92.8	28	6
France	17.6	5	4
Germany	16.6	5	3
UK	10.8	3	3
Italy	10.5	3	7
Japan	31.3	10	(3)
Asia Pacific	23.3	7	14
Latin America	15.9	5	21
Middle East, Africa	11.3	3	13
Canada	8.3	3	19
Total	327.9	100	8

Growth in the US market has increased to 9%, but it still represents 44% of the global prescription pharmaceutical market compared with 30% a decade ago.

At 30th September 2006, GSK held second position in the world pharmaceutical market with a market share of 6.3%, behind Pfizer with a market share of 8%. GSK had six of the world's top 60 pharmaceutical products. These were *Avandia*, *Lamictal*, *Seretide/Advair*, *Valtrex*, *Wellbutrin* and *Zofran*.

World market – top five therapeutic classes	Value £bn	% of total	CER%	Growth £%
Cardiovascular	54.5	17	6	7
Central nervous system	54.0	16	7	8
Alimentary tract and metabolic	39.8	12	7	9
Anti-infectives (bacterial, viral and fungal) excluding vaccines	33.2	10	1	3
Respiratory	21.7	7	5	6

(Note: data based on 12 months to 30th September 2006.)

Products and competition

Pharmaceutical products

GlaxoSmithKline's principal pharmaceutical products are currently directed to eight main therapeutic areas. An analysis of sales by these therapeutic areas, and a description of the principal products, are set out below:

Turnover by therapeutic area	2006 £m	2005 £m	2004 £m
Respiratory	4,995	5,054	4,394
Central nervous system	3,642	3,219	3,462
Anti-virals	2,827	2,598	2,359
Metabolic	1,875	1,495	1,251
Vaccines	1,692	1,389	1,194
Cardiovascular and urogenital	1,636	1,331	932
Anti-bacterials/anti-malarials	1,369	1,519	1,547
Oncology and emesis	1,069	1,016	934
Other	973	1,040	1,027
	20,078	18,661	17,100

Products and all their formulations may not be approved for all indications in all markets where they are available.

Respiratory

Seretide/Advair, a combination of *Serevent* and *Flixotide*, offers a long-acting bronchodilator and an anti-inflammatory in a single inhaler. It is approved for the treatment of asthma and COPD.

Flixotide/Flovent and *Becotide/Beclovent* are inhaled steroids for the treatment of inflammation associated with asthma and COPD.

Serevent is a long-acting bronchodilator used to treat asthma and COPD, and *Ventolin* is a selective short-acting bronchodilator used to treat bronchospasm.

Flixonase/Flonase and *Beconase* are steroid intra-nasal preparations for the treatment of perennial and seasonal rhinitis.

Central nervous system (CNS)

Seroxat/Paxil is a selective serotonin re-uptake inhibitor (SSRI) for the treatment of major depressive disorder, panic, obsessive compulsive disorder, post traumatic stress disorder, social anxiety disorder, and generalised anxiety disorder. A controlled release formulation, *Paxil CR*, is also available in the USA.

Wellbutrin is an anti-depressant, available in the USA and some international markets in normal, sustained-release (SR) and once-daily (XL) formulations.

Migran/Imitrex is a 5HT₁ receptor agonist used for the treatment of severe or frequent migraine and cluster headache and has become the reference product in this sector. *Naramig/Amerge* is also a 5HT₁ receptor agonist indicated for the treatment of migraine.

Lamictal, a well established treatment for epilepsy, is also indicated for bipolar disorder.

Requip is a specific dopamine D₂/D₃ receptor agonist indicated for the treatment of Parkinson's disease and Restless Legs Syndrome (RLS).

Anti-virals

Combivir, a combination of *Retrovir* and *Epivir*, has consolidated the position of these two reverse transcriptase inhibitors as the cornerstone of many multiple anti-HIV product regimens. Physician acceptance has clearly demonstrated the value placed on minimising the pill burden faced by patients.

Ziagen is a reverse transcriptase inhibitor. The product's potency, ease of use and resistance profile allow it to play a significant role in a variety of highly active, well tolerated and simplified HIV treatment regimens.

Trizivir is a combination of *Combivir* and *Ziagen*, combining three anti-HIV therapies in one tablet, for twice daily administration.

Epzicom/Kivexa, approved for use in the USA and Europe, is a combination of *Epivir* and *Ziagen* that is taken as one tablet with once-daily dosing for HIV/AIDS in combination with at least one other anti-HIV drug.

Lexiva/Telzir is a protease inhibitor for the treatment of HIV that is well tolerated and more convenient than *Agenerase*, which it supersedes. *Lexiva* may be taken twice daily or once daily when boosted with ritonavir.

Zeffix has been approved for marketing in the USA, Europe, China and other markets for the treatment of chronic hepatitis B.

Valtrex is a treatment for episodic genital herpes as well as the long term suppression and reduction of transmission of genital herpes, zoster (shingles), cold sores and chicken pox. *Valtrex* supersedes *Zovirax*, which is also used to treat herpes infections.

Metabolic

Avandia is a potent insulin sensitising agent which acts on the underlying pathophysiology of type 2 diabetes.

Avandamet is a combination of *Avandia* and metformin HCl, it is the first medicine that targets insulin resistance and decreases glucose production in one convenient pill.

Avandaryl is a combination of *Avandia* and Amaryl, a Sanofi-Aventis product. *Avandaryl* targets insulin resistance and stimulates pancreatic insulin production.

Bonviva/Boniva is a long-acting bisphosphonate available in once-monthly oral and quarterly injection forms for the treatment of osteoporosis.

Vaccines

GSK markets over 30 vaccines worldwide, of which more than half are combination vaccines to protect children, adolescents and/or adults against up to six diseases at the same time.

Infanrix is GSK's range of paediatric vaccine combinations. *Infanrix* provides protection against diphtheria, tetanus and pertussis (whooping cough). *Infanrix penta* (Europe)/*Pediarix* (USA, Canada) provides additional protection against hepatitis B and polio, and *Infanrix hexa* further adds protection against *Haemophilus influenzae* type b, which is a cause of meningitis. In the USA, *Boostrix* is available to add protection against pertussis (whooping cough) to the routine tetanus/diphtheria booster administered to teenagers.

In GSK's hepatitis vaccines range, *Havrix* protects against hepatitis A and *Engerix-B* against hepatitis B.

Products and competition

continued

Twinrix is the only available combined hepatitis A and B vaccine, protecting against both diseases with one vaccine and available in both adult and paediatric strengths. In Europe, *FENDrix*, a vaccine to prevent hepatitis B in patients with renal insufficiency including high-risk groups such as pre-haemodialysis and haemodialysis patients, is available from 15 years of age onwards.

GSK added *Fluviral* to its portfolio of products when it acquired the Canadian vaccine manufacturer ID Biomedical Corporation in December 2005. *Fluviral* is marketed in Canada. In 2006, the same 'flu vaccine was approved by the US Food and Drug Administration (FDA) for the active immunisation of adults 18 years and older against influenza disease under the brand *FluLaval*. *Fluviral* and *FluLaval* add to *Fluarix* GSK's seasonal 'flu vaccine, which is distributed in 79 countries including the USA.

GSK also markets *Priorix*, a measles, mumps and rubella vaccine, *Typherix*, a vaccine for protection against typhoid fever, and *Varilrix*, a vaccine against varicella or chicken pox. *Priorix-Tetra*, GSK's new combination vaccine to prevent measles, mumps, rubella and varicella (MMRV) was first launched in Germany in August 2006. In addition, the Group markets a range of vaccines to prevent meningitis under the umbrella name *Mencevax*. GSK's new Hib-MenC vaccine, *Menitorix* is now available in the UK. GSK's meningitis vaccine portfolio will be complemented by new meningitis conjugate vaccines in the near future.

As part of its paediatric franchise, GSK continued to roll out the launch of its vaccine against rotavirus induced gastroenteritis, *Rotarix* which is now launched in 90 countries worldwide. Rotavirus vaccination has been included in the national vaccination calendar of five Latin American countries where *Rotarix* will be available free at public health clinics, as part of governmental paediatric immunisation programmes.

Cardiovascular and urogenital

Coreg is an alpha/beta blocker which has been proven to be effective in treating patients with mild, moderate and severe heart failure, heart attack or hypertension. GSK has sole marketing rights in the USA and Canada. Generic versions of the product are available in Canada.

Levitra is a PDE-5 inhibitor indicated for male erectile dysfunction. GSK has co-promotion rights in the USA and more than 20 other markets.

Avodart is a 5-ARI inhibitor currently indicated for benign prostatic hyperplasia. A large clinical outcome study is underway examining its efficacy in the prevention of prostate cancer.

Arixtra, a selective Factor Xa inhibitor, is indicated for the prophylaxis of deep vein thrombosis, which may lead to pulmonary embolism, in hip fracture surgery, knee replacement, hip replacement surgery and abdominal surgery. It is also indicated for the treatment of deep vein thrombosis and pulmonary embolism.

Fraxiparine is a low-molecular weight heparin indicated for prophylaxis of thromboembolic disorders (particularly deep vein thrombosis and pulmonary embolism) in general surgery and in orthopedic surgery, treatment of deep vein thrombosis and prevention of clotting during hemodialysis.

Integrilin is a GP IIb/IIIa inhibitor, approved in the EU for the prevention of early myocardial infarction in patients with unstable angina or non-Q-wave MI.

Anti-bacterials and anti-malarials

Augmentin is a broad-spectrum antibiotic suitable for the treatment of a wide range of common bacterial infections and is particularly effective against respiratory tract infections. *Augmentin ES-600* is an extra strength suspension specifically designed to treat children with recurrent or persistent middle ear infections. *Augmentin XR* is an extra strength tablet form for adults to combat difficult to treat infections.

Ceftin/Zinnat is an oral antibiotic used primarily for community-acquired infections of the lower respiratory tract.

Malarone is an oral anti-malarial used for the treatment and prophylaxis of malaria caused by *Plasmodium falciparum*.

Lapdap is an effective and well tolerated therapy for the treatment of malaria, which has been developed through a public/private collaboration.

Oncology and emesis

Zofran is used to prevent nausea and vomiting associated with chemotherapy and radiotherapy for cancer, and is available in both oral and injectable forms. It is also approved for use in the prevention and treatment of post-operative nausea and vomiting.

Hycamtin is a second line treatment for ovarian, cervical and small cell lung cancer.

Bexxar is a treatment for patients with CD20 follicular, non-Hodgkin's lymphoma with and without transformation whose disease is refractory to rituximab and who have relapsed following chemotherapy.

Arranon (nelarabine) a treatment for patients with T-cell acute lymphoblastic leukaemia and T-cell lymphoblastic lymphoma, received US approval in 2005 and was submitted for European approval in 2006.

Other

This category includes *Betnovate*, the higher potency *Dermovate* and the newer *Cutivate*, which are anti-inflammatory steroid products used to treat skin diseases such as eczema and psoriasis, *Relafen*, a non-steroidal anti-inflammatory drug for the treatment of arthritis, and *Zantac*, for the treatment of peptic ulcer disease and a range of gastric acid related disorders.

Pharmaceuticals competition

The pharmaceutical industry is highly competitive. GSK's principal competitors range from small to large pharmaceutical companies often with substantial resources. Some of these companies and their major products are mentioned below.

Pharmaceuticals may be subject to competition from other products during the period of patent protection and, once off patent, from generic versions. The manufacturers of generic products typically do not bear significant research and development or education and marketing development costs and consequently are able to offer their products at considerably lower prices than the branded competitors. A research and development based pharmaceutical company will normally seek to achieve a sufficiently high profit margin and sales volume during the period of patent protection to repay the original investment, which is generally substantial, and to fund research for the future. Competition from generic products generally occurs as patents in major markets expire. Increasingly patent challenges are made prior to patent expiry, claiming that the innovator patent is not valid and/or that it is not infringed by the generic product. Following the loss of patent protection, generic products rapidly capture a large share of the market, particularly in the USA.

GSK believes that remaining competitive is dependent upon the discovery and development of new products, together with effective marketing of existing products. Within the pharmaceutical industry, the introduction of new products and processes by competitors may affect pricing levels or result in changing patterns of product use. There can be no assurance that products will not become outmoded, notwithstanding patent or trademark protection. In addition, increased government and other pressures for physicians and patients to use generic pharmaceuticals, rather than brand-name medicines, may increase competition for products that are no longer protected by patent.

Respiratory

GSK's respiratory franchise is driven by the growth of *Seretide/Advair*. Major respiratory competitors are Singulair from Merck, especially in the USA, Symbicort from AstraZeneca and Spiriva from Pfizer/Boehringer Ingelheim.

CNS disorders

Major competitors in the USA to *Paxil* are its generic forms, as well as generic fluoxetine, the generic form of Eli Lilly's Prozac, generic sertraline, the generic form of Pfizer's Zoloft, Cymbalta from Eli Lilly, Forest Laboratories' Celexa and Lexapro, and Effexor XR from Wyeth. The principal competitors in the USA for *Wellbutrin* are generic forms of bupropion, the generic forms of SSRIs, Lexapro, Effexor XR, and Cymbalta. *Paxil CR* and the once-daily *Wellbutrin XL* help to retain a strong presence in the anti-depressant market, given the availability of both generic paroxetine and bupropion in the USA. Generic competition for *Seroxat/Paxil* has also occurred in a number of other markets.

The major competitors for *Lamictal* in epilepsy are J&J's Dilantin and generic phenytoin, Novartis's Tegretol/Tegretol XR and generic carbamazepine. UCB's Keppra and Abbot's Depakote/Depakote ER. In Bipolar the major competitors are generic Lithium, other anti-epileptics including Abbott's Depakote/Depakote ER and the atypical anti-psychotics including AstraZeneca's Seroquel. The major competitors for *Imitrex/Imigran* are AstraZeneca's Zomig, Merck's Maxalt and Pfizer's Relpax.

Anti-virals

GSK is a pioneer in the HIV market, launching AZT (*Retrovir*) in 1987 and *Epidur* in 1995, which today are available as *Combivir* in a single tablet, a cornerstone of HIV combination therapy. The launches of *Ziagen*, *Agenerase*, *Trizivir*, *Lexiva* and *Epzicom* have broadened the Group's portfolio of HIV products. Major competitors in the HIV market include Gilead, Bristol Myers Squibb, Abbott, Roche and Boehringer Ingelheim.

Valtrex has strengthened the Group's position in the anti-herpes area, where GSK's *Valtrex* and *Zovirax* compete with Novartis' Famvir. *Valtrex* is a market leader, whilst *Zovirax* faces competition from generic acyclovir. In the hepatitis B market, GSK's *Zeffix* was the first anti-viral on the market. Gilead's Hepsera was the second. The Group has secured marketing rights to *Hepsera* in some key markets.

Metabolic

The major competitor for *Avandia* is Takeda Chemical's Actos, which is co-promoted with Eli Lilly in the USA. Takeda also market ActoplusMet (a combination of Metformin HCl and Actos) in the USA.

Monthly *Boniva/Bonviva* competes with Merck's weekly Fosamax and Proctor & Gamble/Sanofi-Aventis's weekly Actonel. Generic Fosamax (alendronate) is now available in several EU markets including UK and Germany, and also in Canada.

Vaccines

The vaccine market is dominated by five key players. GSK's major competitors include Sanofi Pasteur (SP), Merck, Novartis and Wyeth. Within the paediatric vaccine field, *Infanrix*'s main competitor is SP's range of DTPa-based combination vaccines, although the *Infanrix hexa* combination is the only available hexavalent paediatric combination in Europe.

Cardiovascular and urogenital

GSK markets *Coreg* in the USA where its major competitors are Toprol XL and generic betablockers. *Avodart* competes directly with Merck's Proscar within the BPH market. The Group has co-promotion rights in the USA for *Levitra*, which faces competition from Pfizer's Viagra and Lilly's Cialis.

Anti-bacterials and anti-malarials

Generic versions of both *Augmentin* and *Ceftin/Zinnat* are available in the USA. *Augmentin* also faces generic competition in various European countries. *Augmentin XR* and *Augmentin ES* compete against a broad range of other branded and generic antibiotics. *Malarone*'s safety profile and convenient dosing regimen have helped put this product in a strong position versus mefloquine for malaria prophylaxis.

Oncology and emesis

Zofran provided GSK with a leadership position in the anti-emetic market where competitor companies include Roche, Sanofi-Aventis and more recently MGI and Merck. Generic competitors became available late in 2006. *Zofran* now has full generic competition in the USA. Major competitors in the diverse cytotoxic market include Bristol Myers Squibb, Sanofi-Aventis, Novartis and Roche/Genentech. GSK's cytotoxic portfolio, led by *Hycamtin*, currently holds a relatively small market position.

Products and competition

continued

Consumer Healthcare products

GlaxoSmithKline's principal consumer healthcare products are in three major areas. An analysis of sales by these areas is set out below:

	2006 £m	2005 £m	2004 £m
OTC medicines	1,496	1,437	1,400
Oral care	993	943	913
Nutritional healthcare	658	619	573
	3,147	2,999	2,886

Major products, which are not necessarily sold in all markets, are:

Category	Product
Over-the-counter medicines	
Analgesics	<i>Panadol</i>
Dermatologicals	<i>Zovirax</i> <i>Abreva</i>
External nasal dilators	<i>Breathe Right</i>
Gastro-intestinal	<i>Tums</i> <i>Citrucel</i>
Respiratory tract	<i>Contac</i>
Smoking control	<i>Beechams</i> <i>Commit</i> <i>Nicorette</i> <i>NicoDerm CQ</i> <i>NiQuitin CQ</i> <i>Nicabate CQ</i>
Natural wellness support	<i>Abtei</i>
Oral care	
	<i>Aquafresh</i> <i>Dr Best</i> <i>Macleans</i> <i>Odol</i> <i>Odol Med 3</i> <i>Polident</i> <i>Poligrip</i> <i>Sensodyne</i>
Nutritional healthcare	
	<i>Lucozade</i> <i>Ribena</i> <i>Horlicks</i>

Over-the-counter medicines

The leading products are *Panadol*, a widely available paracetamol/acetaminophen analgesic, *Nicorette* gum in the USA, the *NicoDerm*, *NiQuitin CQ* and *Nicabate* range of smoking control products, *Tums*, a calcium-based antacid, *Citrucel* laxative, *Contac* for the treatment of colds, *Abtei*, a natural medicines and vitamin range, and *Zovirax* and *Abreva* for the treatment of cold sores. In December 2006, the company acquired *Breathe Right* nasal strips that gently lift open nasal passages to provide better breathing, and *FiberChoice* daily fibre supplements, through the acquisition of CNS, Inc.

GSK's portfolio will be strengthened further in 2007 with the US launch of *alli*, a new treatment for weight-loss.

Oral care

The leading Oral care products are toothpastes and mouthwashes under the *Aquafresh*, *Odol*, *Sensodyne* and *Macleans* brand names, and a range of toothbrushes sold under the *Aquafresh* and *Dr Best* names. In addition, denture care products are available principally under the *Polident*, *Poligrip* and *Corega* brand names.

Nutritional healthcare

The leading products in this category are *Lucozade* energy and sports drinks, *Ribena*, a blackcurrant juice-based drink, and *Horlicks*, a range of milk-based malted food and chocolate drinks.

Consumer Healthcare competition

GSK holds leading global positions in all its key consumer product areas. Worldwide it is the third largest in Oral care and in OTC medicines. In Nutritional healthcare it holds the leading position in the UK, India and Ireland.

The environment in which the Consumer Healthcare business operates has become ever more challenging:

- consumers are demanding better quality, better value and improved performance
- retailers have consolidated and globalised which has strengthened their negotiation power
- manufacturers are consolidating, leading to more aggressive competition across all elements of the marketing mix
- cycle times for innovation have reduced.

The main competitors include the major international companies Colgate-Palmolive, Johnson & Johnson, Procter & Gamble, Unilever and Wyeth. In addition, there are many other companies that compete with GSK in certain markets.

The major competitor products in OTC medicines are:

- in the USA: Metamucil (laxative), Pepcid (indigestion) and private label smoking control products
- in the UK: Lemsip (cold remedy), Nurofen and Anadin (analgesics), and Nicorette and Nicotinell (smoking control treatments).

In Oral care the major competitors are Colgate-Palmolive's Colgate and Procter & Gamble's Crest.

In Nutritional healthcare the major competitors to *Horlicks* are Ovaltine and Milo malted food and chocolate drinks. The competitors to *Ribena* are primarily local fruit juice products, while *Lucozade* competes with other energy drinks.

Pharmaceutical turnover

All growth rates included in the review of turnover are at constant exchange rates (CER) unless otherwise stated. The sterling growth rates may be found in the tables of pharmaceutical turnover by therapeutic area on page 32 and by geographic region on page 33. Total pharmaceutical turnover in 2006 was £20,078 million compared with £18,661 million in 2005, an increase of 9% CER. Within the Group's portfolio, turnover of new products first launched in a major market within the last five years accounted for 27% (2005 – 24%) of total turnover and grew by 20% to £5,333 million (2005 – £4,478 million). Turnover of the more established, franchise products amounted to £11,709 million (2005 – £10,933 million), representing 58% of total turnover, and increased 9% compared with last year. Turnover of older products, now less actively promoted, was £3,036 million (2005 – £3,250 million), representing 15% of total turnover, and declined by 5%. In sterling terms total pharmaceutical turnover increased 8%, 1% less than CER due principally to the strength of Sterling against major International currencies.

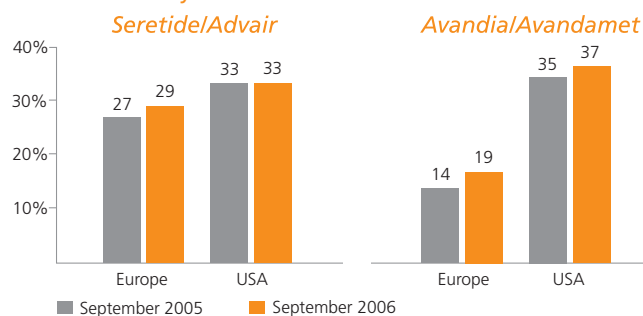
Pharmaceutical turnover by therapeutic area

GSK's ability in 2006 to deliver continued pharmaceutical turnover growth was primarily due to an exceptionally broad product portfolio of high-value growth products coupled with sales and marketing excellence. These growth products include *Seretide/Advair*, the *Avandia* product group, Vaccines, *Lamictal*, *Valtrex*, *Coreg*, *Requip*, *Avodart* and *Boniva*.

Respiratory

GSK continues to be the global leader in respiratory pharmaceuticals with sales of its three key products, *Seretide/Advair*, *Flixotide/Flovent* and *Serevent* amounting to £4.3 billion, up 9%. Total sales of *Seretide/Advair*, for asthma and COPD, rose 11% to £3.3 billion. In the USA, sales grew 13% to £1.9 billion. In Europe, sales grew 10% to £1.1 billion and in International markets, sales grew 9% to over £300 million. Market share by value in the anti-asthma and COPD therapy class was 29% in Europe and 33% in the USA, an increase of 2 percentage points in Europe and a flat market share growth in the USA (reflecting lower prescription volumes due to a label change in early 2006 that restricted GSK's ability to promote the product, offset by favourable pricing changes).

Market share by value



The positive results of the TOwards a Revolution in COPD Health (TORCH) study, the largest of its kind, were filed with regulators early in 2007 and in February were published in the 'New England Journal of Medicine'. The results of the three year study, sponsored by GSK, showed important benefits of *Seretide* in the treatment of patients with COPD.

Central nervous system (CNS)

CNS sales increased 15% to £3.6 billion. Sales increased in the USA and International, but declined in Europe due to generic competition. Total *Seroxat/Paxil* sales grew 4% to £620 million, due to strong growth of *Paxil CR* in the USA and *Paxil IR* in Japan partly offset by generic competition to *Paxil IR* in Europe.

Total *Wellbutrin* sales grew 24% to £900 million. Sales of *Wellbutrin XL*, a once-daily product, grew 25% to £798 million. In December 2006, generic competition to the *Wellbutrin XL* 300mg tablet (approximately 60% of *Wellbutrin* sales) entered the US market.

Sales of *Lamictal*, for the treatment of epilepsy and bipolar disorder, grew 19% to just under £1 billion, benefiting from its new indication to treat one of the most serious forms of epilepsy – primary generalised tonic-clonic seizures. *Lamictal* is also the only medicine with long-term clinical data that demonstrates that it can delay the onset of depressive episodes of bipolar disorder. In November, GSK submitted *Lamictal XR*, a new once daily treatment, to the FDA for treatment of epilepsy. The company intends to present data on *Lamictal XR* at the American Academy of Neurology meeting in April 2007.

Sales of *Requip*, for Parkinson's disease and Restless Legs Syndrome (RLS), grew 74% to £268 million and, in December, the FDA accepted GSK's file for approval of the new formulation *Requip CR*.

Anti-virals

Total sales of HIV products were £1.5 billion, down 1%. Competition to older products, *Combivir* down 9% to £528 million and *Epivir* down 21% to £202 million, was mostly offset by strong sales growth of new products *Epzicom/Kivexa* which more than doubled to £241 million and *Lexiva/Agenerase* up 18% to £131 million.

Sales of *Valtrex*, rose 24% to £845 million, with US sales up 30% to £600 million driven by patients switching to suppression therapy.

Metabolic

GSK launched *Avandia* for the treatment of type 2 diabetes in 1999 and a combination product, *Avandamet*, for blood sugar control in 2002. The product group was expanded further in February 2006 with the launch in the USA of a fixed-dose combination treatment, *Avandaryl*, which combines *Avandia* with a sulfonylurea.

In 2006, sales of the *Avandia* product group grew 24% to £1.2 billion in the USA. In Europe, sales grew 39% to £217 million driven by the increasing use of *Avandamet*. Sales in International markets rose 17% to £234 million. The *Avandia* product group achieved in 2006 a market share by value in oral anti-diabetics of 37% in the USA and 19% in Europe, up 2 and 5 percentage points, respectively. In the USA, *Avandamet* prescription volume growth was adversely impacted by product supply issues during the year which have now been resolved.

In December, GSK presented data from the landmark ADOPT study, which demonstrated that *Avandia* is more effective than metformin, or a sulphonylurea, in long-term blood sugar control in type 2 diabetes. These data are in addition to those recently presented from the DREAM study, which showed that *Avandia* can reduce the risk of progression to type 2 diabetes. Data from both these studies are expected to be filed with regulatory agencies during the first half of 2007.

GSK recorded in turnover a £95 million share of co-promotion income for *Boniva/Bonviva*, a new once-monthly oral bisphosphonate for the treatment of postmenopausal osteoporosis, which was developed with Roche, and launched in 2005.

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Pharmaceutical turnover by therapeutic area 2006

Therapeutic area/ major products	% of total	2006 £m	2005 £m	Total		USA			Europe			International		
				Growth CER% £%	2006 £m	Growth CER% £%	2006 £m	Growth CER% £%	2006 £m	Growth CER% £%				
Respiratory	27	4,995	5,054	–	(1)	2,461	(3)	(5)	1,697	3	2	837	4	3
Seretide/Advair		3,313	3,003	11	10	1,870	13	11	1,133	10	10	310	9	10
Flixotide/Flovent		659	638	5	3	298	16	14	173	(8)	(8)	188	2	–
Serevent		291	330	(10)	(12)	86	(16)	(17)	140	(13)	(13)	65	5	(2)
Flixonase/Flonase		311	656	(52)	(53)	184	(63)	(64)	51	(15)	(15)	76	(14)	(16)
Central Nervous System	17	3,642	3,219	15	13	2,588	28	26	595	(15)	(15)	459	2	(1)
Seroxat/Paxil		620	615	4	1	175	35	32	149	(20)	(20)	296	5	–
Paxil IR		448	488	(5)	(8)	19	11	6	149	(20)	(20)	280	4	(1)
Paxil CR		172	127	37	35	156	38	36	–	–	–	16	25	33
Wellbutrin		900	739	24	22	882	24	22	2	–	–	16	7	14
Wellbutrin IR, SR		102	92	12	11	89	14	11	2	–	–	11	–	10
Wellbutrin XL		798	647	25	23	793	25	23	–	–	–	5	25	25
Imigran/Imitrex		711	697	3	2	551	11	9	118	(18)	(18)	42	(12)	(14)
Lamictal		996	849	19	17	765	37	35	175	(22)	(23)	56	2	2
Requip		268	156	74	72	176	>100	>100	81	21	19	11	25	38
Anti-virals	14	2,827	2,598	10	9	1,354	7	5	855	11	11	618	16	14
HIV		1,515	1,554	(1)	(3)	700	(7)	(9)	621	3	2	194	8	7
Combivir		528	583	(9)	(9)	238	(14)	(16)	217	(4)	(4)	73	–	–
Trizivir		268	303	(11)	(12)	141	(13)	(15)	113	(7)	(8)	14	(7)	–
Epivir		202	261	(21)	(23)	69	(25)	(26)	90	(26)	(26)	43	(2)	(7)
Ziagen		117	136	(13)	(14)	48	(11)	(13)	41	(24)	(24)	28	4	4
Agenerase, Lexiva		131	112	18	17	74	7	6	48	40	37	9	14	29
Epizicom/Kivexa		241	118	>100	>100	125	49	47	97	>100	>100	19	>100	>100
Herpes		965	826	19	17	610	30	28	144	4	4	211	3	–
Valtrex		845	695	24	22	600	30	28	109	12	11	136	10	7
Zovirax		120	131	(6)	(8)	10	67	67	35	(15)	(15)	75	(7)	(11)
Zeffix		162	145	12	12	13	8	8	23	10	10	126	13	13
Relenza		91	5	>100	>100	–	–	–	62	>100	>100	29	>100	>100
Metabolic	8	1,875	1,495	27	25	1,277	30	28	252	33	33	346	12	12
Avandia		1,399	1,154	23	21	1,068	26	24	125	13	12	206	13	16
Avandamet		204	175	17	17	86	(22)	(24)	92	>100	>100	26	41	53
Avandaryl		42	–	–	–	40	–	–	–	–	–	2	–	–
Bonviva/Boniva		95	18	>100	>100	83	>100	>100	12	>100	>100	–	–	–
Vaccines	8	1,692	1,389	23	22	465	40	38	709	20	20	518	13	13
Hepatitis		479	444	9	8	161	21	18	227	2	2	91	8	10
Infanrix, Pediarix		511	431	29	28	172	20	18	281	40	39	58	12	12
Boostrix		60	29	>100	>100	41	>100	>100	15	88	88	4	67	33
Cardiovascular and urogenital	7	1,636	1,331	24	23	1,072	42	40	395	(4)	(5)	169	13	13
Coreg		779	573	38	36	773	38	36	–	–	–	6	20	20
Levitra		43	40	8	8	41	20	17	1	(75)	(75)	1	–	–
Avodart		216	129	69	67	131	>100	>100	69	25	25	16	67	78
Arixtra		58	24	>100	>100	32	>100	>100	23	>100	>100	3	>100	>100
Fraxiparine		209	211	(1)	(1)	–	–	–	179	–	–	30	(6)	(6)
Anti-bacterials	8	1,369	1,519	(9)	(10)	217	(15)	(17)	628	(12)	(13)	524	(2)	(3)
Augmentin		570	666	(14)	(14)	94	(31)	(32)	268	(15)	(15)	208	–	(1)
Zinnat/Ceftin		164	197	(16)	(17)	12	20	20	82	(27)	(27)	70	(5)	(7)
Oncology & emesis	5	1,069	1,016	7	5	836	12	10	153	(7)	(7)	80	(11)	(12)
Zofran		847	837	3	1	679	8	6	107	(14)	(14)	61	(16)	(18)
Hyccantin		113	99	15	14	72	11	9	34	26	26	7	17	17
Other	6	973	1,040	(5)	(6)	83	19	19	263	(19)	(18)	627	(1)	(3)
Zantac		232	244	(2)	(5)	72	28	24	52	(19)	(19)	108	(7)	(11)
	100	20,078	18,661	9	8	10,353	16	14	5,547	1	–	4,178	6	4

CER% represents growth at constant exchange rates. £% represents growth at actual exchange rates. Turnover by quarter is given in the Financial record on pages 174 to 177.

Vaccines

Overall vaccine sales increased 23% to £1.7 billion, with good performances from all regions: US sales rose 40% to £465 million; European sales grew 20% to £709 million and sales in International were up 13% to £518 million. Key contributors were: *Infanrix/Pediarix*, GSK's combination vaccines for children, with sales up 29% to £511 million; and sales of hepatitis vaccines, which grew 9% to £479 million, benefiting from a strong US performance of *Havrix*, following approval last year for broader paediatric use.

Sales of new vaccines also helped drive overall sales growth. Total sales of *Rotarix*, for rotavirus, *Boostrix*, for prevention of diphtheria, tetanus and whooping cough, and influenza vaccines, *Fluarix/FluLaval*, reached £274 million, up 91%. This was the first full year sales of *FluLaval* following the acquisition of ID Biomedical in late 2005.

Oncology and emesis

Sales of *Zofran* grew 3% to £847 million, driven by the US market, up 8% to £679 million. Europe and International sales declined 14% and 16% respectively due to generic competition. A generic competitor to *Zofran* entered the US market in November 2006.

Cardiovascular and urogenital

Sales of *Coreg*, for heart disease, grew 38% to £779 million. *Avodart*, for benign prostatic hyperplasia (enlarged prostate), had a very strong year, with sales increasing 69% to £216 million.

Anti-bacterials

Anti-bacterial sales declined 9% reflecting generic competition and a weaker 'flu season.

Other therapeutic areas

Sales of *Zantac* fell 2% to £232 million, with declines in Europe and International partially offset by a 28% growth in the USA.

Regional analysis

Pharmaceutical turnover by geographic region in 2006 on an invoiced basis

The turnover reported in the table below represents sales invoiced by GSK's local entity to its customers in the local market plus co-promotion income within each market.

Region/ major markets	% of total	2006 £m	2005 £m	Growth* CER%	Growth* £%
USA	52	10,353	9,106	16	14
Europe	27	5,547	5,537	1	-
France		967	975	-	(1)
UK		788	762	3	3
Italy		665	662	1	-
Germany		595	554	8	7
Spain		577	586	(1)	(2)
Other Europe		1,955	1,998	(2)	(2)
International	21	4,178	4,018	6	4
Asia Pacific		1,377	1,324	4	4
Japan		860	854	8	1
Middle East, Africa		744	746	3	-
Latin America		714	651	10	10
Canada		483	443	4	9
	100	20,078	18,661	9	8

*CER% represents growth at constant exchange rates. £% represents growth at actual exchange rates.

Individual governments determine the pricing of medicines in most countries within Europe, which can result in wide price variations for the same product. Parallel trade occurs when third parties exploit this price differential by purchasing products in markets where low prices are enforced and selling them to governments and other purchasers in those markets where higher prices have been agreed. This parallel trade is permitted under the single market rules in the European Union. GSK does not derive any benefit from the profit on resale at the higher price.

As a result, management believes that within the European region, turnover by market, on an invoiced basis as presented above, does not properly represent the consumption of the products within each market. GSK employees based in each market are instrumental in the promotion of the Group's products within their market, thereby creating a product sale and final consumption in that market.

The following table gives the adjustments made in order to restate the turnover for markets within Europe on a turnover created basis.

Pharmaceutical turnover for Europe region in 2006 on a turnover created basis

Region/ major markets	2006			2005		
	Invoiced £m	Adjustment £m	Created £m	Invoiced £m	Adjustment £m	Created £m
Europe	5,547	-	5,547	5,537	-	5,537
France	967	(66)	901	975	(47)	928
UK	788	101	889	762	91	853
Italy	665	(25)	640	662	(13)	649
Germany	595	71	666	554	57	611
Spain	577	(14)	563	586	(15)	571
Other Europe	1,955	(67)	1,888	1,998	(73)	1,925

These adjustments are GSK's estimates based on the most recent data from independent external sources, valued in Sterling at relevant exchange rates. Management believes that this turnover created basis of reporting turnover by market provides a better reflection of the performance of the businesses in each market within Europe.

The total turnover for the Europe region is unaffected by this restatement.

Parallel trade occurs occasionally elsewhere in the world, but it is not sufficiently material to affect significantly the turnover data by market presented on an invoiced basis.

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Pharmaceutical turnover by geographic region in 2006 on a turnover created basis

Turnover by market within Europe has been adjusted for the effects of parallel trade to show turnover on the basis of the country where the product is finally consumed, not where the product was sold by GSK.

Region/ major markets	% of total	2006 £m	2005 £m	Growth*	
				CER%	£%
USA	52	10,353	9,106	16	14
Europe	27	5,547	5,537	1	-
France		901	928	(2)	(3)
UK		889	853	4	4
Italy		640	649	(1)	(1)
Germany		666	611	10	9
Spain		563	571	(1)	(1)
Other Europe		1,888	1,925	(2)	(2)
International	21	4,178	4,018	6	4
Asia Pacific		1,377	1,324	4	4
Japan		860	854	8	1
Middle East, Africa		744	746	3	-
Latin America		714	651	10	10
Canada		483	443	4	9
	100	20,078	18,661	9	8

* CER% represents growth at constant exchange rates. £% represents growth at actual exchange rates. Turnover by quarter is given in the Financial record on pages 174 to 177.

USA

A strong sales performance in the USA, up 16% to £10.4 billion, was the main contributor to total pharmaceutical turnover growth of 9% in 2006.

Advair sales grew 13% to £1,870 million. *Flovent* sales increased by 16%. *Flonase*, indicated for the treatment of perennial rhinitis, declined 63% following the launch of a generic competitor in Q1 2006.

Sales of *Wellbutrin* products grew 24% to £882 million reflecting the performance of *Wellbutrin XL*, a new once-daily product, which grew 25% to £793 million.

Total sales of *Paxil* were up 35% to £175 million largely due to the rectification of supply issues experienced in 2005 at the Cidra plant in Puerto Rico.

Sales in the anti-virals therapeutic area grew 7% with HIV products down 7% and herpes products up 30%. Competition to older products, *Combivir* down 14% and *Epivir* down 25%, was partly offset by the growth of new products *Epzicom/Kivexa* up 49% and *Lexiva* up 7%. *Valtrex*, for herpes, grew 30% to £600m driven by patients switching to suppression therapy.

Sales of the *Avandia* product group increased by 24% reflecting the re-supply of product following supply disruption at the Cidra plant in Puerto Rico in 2005 and price increases.

Vaccines grew 40% reflecting the good performance of *Pediarix* and *Boostrix*, *Fluarix* and the launch of *Flulaval* in 2006.

Coreg sales increased 38% to £773 million as it continued to benefit from its wide range of indications in heart disease. *Zofran* sales increased 8% to £679 million. A generic competitor to *Zofran* entered the market in November 2006.

Anti-bacterial sales declined 15% as a result of generic competition.

Europe

The discussion of individual market performance in the Europe region is on a turnover created basis.

Sales in Europe contributed 27% of pharmaceutical turnover and grew 1%, to over £5.5 billion, with strong sales from *Seretide*, *Avandia/Avandamet* and vaccines offsetting the impact of generic competition to a number of products and continued price cuts resulting from government healthcare reforms.

Markets which recorded good growth included Germany, the UK, Central and South/East Europe whilst growth in France, the Netherlands, Poland, Italy and Spain was adversely impacted by pricing and generics.

Major growth drivers were *Seretide*, GSK's largest selling product in Europe, with growth of 10%, *Avandia/Avandamet* which grew 39%, and the vaccines franchise, up 20%. Sales of anti-virals grew 11% primarily due to government orders of *Relenza* as a measure in the event of a potential 'flu pandemic.

Generic competition negatively impacted sales of *Seroxat* down 20%, *Lamictal* down 22%, *Zofran* down 14% and *Imigran*, down 18%. Sales of anti-bacterials decreased 12% due to a combination of a weaker 'flu season than in 2005 and generic competition.

International

The International region reported year on year turnover growth of 6%. Strong growth in Japan, up 8% (despite the biennial price reductions), China/Hong Kong, up 7% and Latin America, up 10%, was partly offset by modest sales growth of 4% in Canada and 3% in Australia. The Canadian sales performance reflected generic competition for *Imigran* and *Zofran* whilst the Australian business was negatively impacted by Government pricing reforms and generic competition to *Lamictal* and *Paxil*.

The performance in Japan was driven by the sales of *Paxil*, up 15%, *Serevent*, up 16% and Anti-virals, up 8% and the full year impact of *Zyrtec*, an allergy product in-licensed from UCB in 2005. These were partially offset by declines in the older products *Zantac* and *Zovirax*. *Flonase* also declined due to a low pollen season.

Across all markets in International, the key products driving growth were *Seretide*, which grew 9% to record sales of £310 million, the *Avandia* range of products which grew 17% to £234 million, HIV products which grew 8% and the vaccines franchise, which recorded growth of 13% and achieved sales of £518 million.

Consumer Healthcare sales

An analysis of Consumer Healthcare sales is set out in the following table:

	2006		2005		Growth	
	£m		£m		CER%	£%
OTC medicines	1,496		1,437		5	4
Analgesics	380		362		7	5
Dermatological	165		161		4	2
Gastro-intestinal	252		249		2	1
Respiratory tract	172		154		12	12
Smoking control	353		336		7	5
Natural wellness support	132		133		–	(1)
Oral care	993		943		6	5
Nutritional healthcare	658		619		7	6
	3,147		2,999		6	5

Consumer Healthcare sales grew 6% to £3.1 billion, with sales in International up 10% and Europe up 7%, performing well. Total sales in the USA were flat, with an improved performance in the fourth quarter, with sales up 7%.

OTC medicines

Over-the-counter medicine sales grew 5% to £1.5 billion with *Panadol* and smoking control performing well.

Oral care

Oral care sales grew 6% to £993 million. *Sensodyne* grew strongly, up 19% for the year to £257 million. Sales of *Aquafresh* were down 3% to £283 million.

Nutritional healthcare

Nutritional healthcare products sales grew 7% to £658 million. *Lucozade*, grew 14% to £301 million, and *Horlicks*, grew 6% to £156 million. *Ribena* sales were down 1% to £169 million.

Operating profit

The analysis below of operating profit and subsequent discussion compares the 2006 results with 2005 results.

	2006		2005		Growth	
	£m	%	£m	%	CER%	£%
Turnover	23,225	100.0	21,660	100.0	9	7
Cost of sales	(5,010)	(21.6)	(4,764)	(22.0)	6	5
Selling, general and administration	(7,257)	(31.2)	(7,250)	(33.5)	–	–
Research and development	(3,457)	(14.9)	(3,136)	(14.5)	11	10
Other operating income	307	1.3	364	1.7		
Operating profit	7,808	33.6	6,874	31.7	17	14

Cost of sales

Cost of sales declined as a percentage of turnover by 0.4 percentage points. At constant exchange rates the decline was 0.6 percentage points reflecting favourable price and regional mix impact.

Selling, general and administration

Selling, general and administration (SG&A) costs as a percentage of turnover reduced 2.3 percentage points. At constant exchange rates, the decrease was 2.5 percentage points, reflecting flat expenditure compared with prior year on a turnover growth of 9%. SG&A costs were flat due to higher advertising, promotion and selling expenditure offset by lower general and administration expenditure. Advertising, promotion and selling increased 3% and accounted for a 2% increase in total SG&A. General and administration expenditure declined 5% and accounted for a 2% decline in total SG&A, of which one percentage point was due to lower charges related to legal matters and one percentage point was due to lower costs related to programmes to deliver future cost savings.

Research and development

R&D expenditure increased 11% partly as a result of higher charges related to restructuring programmes. Excluding restructuring costs R&D grew 8%, broadly in-line with turnover. Pharmaceuticals R&D expenditure, excluding restructuring costs, represented 16.2% (2005 – 16.2%) of pharmaceutical turnover.

Other operating income

Other operating income includes royalty income, equity investment disposals and impairments, product disposals and fair value adjustments to the Quest collar and Theravance options. Other operating income was £307 million in 2006 compared with £364 million in 2005. The decrease is primarily due to lower product and asset disposal profits partially offset by the favourable fair value movement to the Quest collar and Theravance options.

Operating profit

Overall, the operating profit margin increased 1.9 percentage points as operating profit increased 14% in sterling terms to £7,808 million. Operating profit increased 17% at constant exchange rates and the margin increased 2.4 percentage points, reflecting SG&A growth below the rate of turnover growth, partially offset by higher costs related to programmes to deliver future cost savings and lower other operating income.

Gains from asset disposals were £169 million (2005 – £290 million), costs for legal matters were £333 million (2005 – £430 million), the fair value movements on the Quest collar and Theravance options resulted in an income of £29 million (2005 – £19 million) and charges relating to cost-saving programmes were £205 million (2005 – £141 million). The total operating profit impact of these items was a £340 million charge in 2006, compared with a £262 million charge in 2005.

Profit before taxation

The discussion below compares the 2006 results with the 2005 results.

Share of profits/(losses) of joint ventures and associated undertakings

The share of profits of associates arises principally from the Group's holding in Quest Diagnostics Inc.

Disposal of interest in associates

There were no disposals of interests in associates in 2006 and 2005. The Group's shareholding in Quest as at 31st December 2006 was 18.7%.

Financial review 2006

continued

Net finance costs

	2006 £m	2005 £m
Finance income		
Interest income	285	276
Fair value adjustments and hedges	2	(19)
	287	257
Finance costs		
Interest costs	(314)	(427)
Unwinding of discount on liabilities	(36)	(25)
Fair value adjustments and hedges	(2)	1
	(352)	(451)

Finance income increased compared with 2005 predominantly due to increased income on extended credit on receivables and increased interest income due to higher US dollar interest rates. Finance costs reduced due to the refinancing of two expensive bonds in December 2005 and January 2006 as well as lower swap costs resulting from reduced interest rate differentials.

Taxation

	2006 £m	2005 £m
UK corporation tax	400	172
Overseas taxation	2,310	1,847
Current taxation	2,710	2,019
Deferred taxation	(409)	(103)
Total	2,301	1,916

The charge for taxation on profit amounting to £2,301 million, represents an effective tax rate of 29.5% (2005 – 28.5%). The Group balance sheet at 31st December 2006 included a tax payable liability of £621 million and a tax recoverable asset of £186 million.

As reported last year, GSK's largest unresolved tax issues were with the US Internal Revenue Service (IRS) and UK HM Revenue and Customs (HMRC) in respect of transfer prices related to the Glaxo heritage products.

On 11th September 2006, GSK and the IRS agreed to a resolution of their dispute. Under the agreement, GSK has made gross payments to the IRS of approximately \$3.3 billion. The final net cash cost to the Group is approximately \$3.1 billion, which covers federal, state and local taxes, interest and the benefit of tax relief on the payments made. The settlement resolved all the transfer pricing issues in dispute for the period 1989 – 2000, which were due to go to trial in February 2007, and also covers the subsequent years 2001 – 2005. GSK had previously made provision for the dispute and this settlement did not have any significant impact on the Group's reported earnings or tax rate for the year.

GSK continues to be in dispute with HMRC primarily in respect of transfer pricing and Controlled Foreign Companies legislation matters for the years 1994 to date and the parties are now preparing for litigation. HMRC has not formally quantified its claims in respect of these matters but there continues to be a wide difference between the Group and HMRC positions on these matters.

GSK has open issues in Japan and Canada, which were the subject of court proceedings in 2006. In Japan the tax authorities are claiming approximately Yen 39 billion (£169 million) in respect of transactions in 1998. GSK has paid the tax claimed, as required by law, and applied for a refund. A court decision is expected in late March 2007.

A court decision in the Group's dispute with the Canadian Revenue Authority over the pricing of *Zantac* in the years 1989 – 1993 is expected in the first half of 2007.

GSK uses the best advice in determining its transfer pricing methodology and in seeking to manage transfer pricing issues to a satisfactory conclusion and, on the basis of external professional advice, continues to believe that it has made adequate provision for the liabilities likely to arise from open assessments. The ultimate liability for such matters may vary from the amounts provided and is dependent upon the outcome of litigation proceedings and negotiations with the relevant tax authorities.

Profit for the year

	2006 £m	2005 £m	Growth	
			CER%	£%
Profit after taxation for the year	5,498	4,816	17	14
Profit attributable to shareholders	5,389	4,689	18	15
Earnings per share (pence)	95.5p	82.6p	19	16
Earnings per ADS (US\$)	\$3.53	\$3.00		
Weighted average number of shares (millions)	5,643	5,674		
Diluted earnings per share (pence)	94.5p	82.0p		
Diluted earnings per ADS (US\$)	\$3.50	\$2.98		
Weighted average number of shares (millions)	5,700	5,720		

Profit for the year was £5,498 million, an increase of 17% (14% in sterling terms). Profit attributable to minority interests was £109 million and profit attributable to shareholders was £5,389 million, an increase of 18% (15% in sterling terms). Earnings per share increased 19%, reflecting higher profits and also the reduction in the weighted average number of shares resulting from the Group's share buy-back programme. The interest cost of this programme also adversely impacts the Group's earnings. At actual rates of exchange, earnings per share increased 16%. The unfavourable currency impact on EPS of three percentage points reflects a strengthening of Sterling against other major currencies and compares with a two percentage point unfavourable currency impact on turnover.

Dividend

The Board has declared a fourth interim dividend of 14 pence per share resulting in a dividend for the year of 48 pence, a four pence increase over the dividend of 44 pence per share for 2005. The equivalent interim dividend receivable by ADR holders is 55.1628 cents per ADS based on an exchange rate of £1/\$1.9701. The dividend had an ex-dividend date of 14th February 2007, a record date of 16th February 2007 and will be paid on 12th April 2007. The liability for an interim dividend is only recognised when it is paid, which is usually after the accounting period to which it relates. The 2006 financial statements recognise the dividends paid in 2006, namely the third and fourth interim dividends for 2005 and the first and second interim dividends for 2006, which total £2,598 million (2005 – £2,390 million).

Critical accounting policies

The consolidated financial statements are prepared in accordance with International Financial Reporting Standards, as adopted for use in the European Union, following the accounting policies approved by the Board and described in Note 2 to the financial statements, 'Accounting policies'. Management is required to make estimates and assumptions that affect the amounts of assets, liabilities, revenue and expenses reported in the financial statements. Actual amounts and results could differ from those estimates. The following are considered to be the critical accounting policies adopted.

Turnover

Revenue is recognised when title and risk of loss is passed to the customer and reliable estimates can be made of relevant deductions. Gross turnover is reduced by rebates, discounts, allowances and product returns given or expected to be given, which vary by product arrangements and buying groups. These arrangements with purchasing organisations are dependent upon the submission of claims some time after the initial recognition of the sale. Accruals are made at the time of sale for the estimated rebates, discounts or allowances payable or returns to be made, based on available market information and historical experience. Because the amounts are estimated they may not fully reflect the final outcome, and the amounts are subject to change dependent upon, amongst other things, the types of buying group and product sales mix. The level of accrual is reviewed and adjusted regularly in the light of contractual and legal obligations, historical trends, past experience and projected market conditions. Market conditions are evaluated using wholesaler and other third-party analyses, market research data and internally generated information. Future events could cause the assumptions on which the accruals are based to change, which could affect the future results of the Group.

The Group's largest business is US pharmaceuticals, and the US market has the most complex arrangements for rebates, discounts and allowances. The following briefly describes the nature of the arrangements in existence in the Group's US pharmaceuticals business.

- Customer rebates are offered to key managed care and group purchasing organisations (GPO) and other direct and indirect customers. These arrangements require the customer to achieve certain performance targets relating to value of product purchased, formulary status or pre-determined market shares relative to competitors. Rebates given under Medicare, Part D are included in this category. The Medicare, Part D programme was introduced during 2006 and replaces the Government Medicaid subsidies for some individuals with subsidised coverage provided through private prescription plans. The accrual for these rebates is estimated based on the specific terms in each agreement, historical experience and product growth rates.
- GSK has arrangements with certain key parties, whereby the party is able to buy products from wholesalers at lower prices. A chargeback represents the difference between the invoice price to the wholesaler and the indirect customer's contractual discounted price. Accruals for estimating chargebacks are calculated based on the terms of each agreement, historical experience and product growth rates.

- The US Medicaid programme is a state-administered programme providing assistance to certain poor and vulnerable patients. In 1990, the Medicaid Drug Rebate Program was established to reduce state and federal expenditure on prescription drugs. GSK participates by providing rebates to states. Accruals for Medicaid rebates are calculated based on the specific terms of individual state agreements using a combination of historical experience, product and population growth, anticipated price increases and the impact of contracting strategies.
- Cash discounts are offered to customers to encourage prompt payment. These are accrued for at the time of invoicing and adjusted subsequently to reflect actual experience.
- Where there is historical experience of customer returns, GSK records an accrual for estimated sales returns by applying historical experience of customer returns to the amounts invoiced, together with market related information such as stock levels at wholesalers, anticipated price increases and competitor activity.

A reconciliation of gross turnover to net turnover for the US pharmaceuticals business is as follows:

	2006		2005		2004	
	£m	%	£m	%	£m	%
Gross turnover	13,131	100	11,875	100	10,835	100
Managed care, GPO rebates and Medicare, Part D	912	7	686	6	575	5
Chargebacks	846	6	786	7	732	7
US Government and State programmes	507	4	775	6	734	7
Cash discounts	248	2	227	2	208	2
Customer returns	140	1	155	1	86	1
Prior year adjustments	(69)	–	(34)	–	(51)	(1)
Other items	194	1	174	1	126	1
Total deductions	2,778	21	2,769	23	2,410	22
Net turnover	10,353	79	9,106	77	8,425	78

Rebates given under the US Government Medicaid programme have fallen in 2006 and been replaced with rebates granted under the Medicare, Part D programme. The overall level of rebates has fallen slightly, partly as a result of products with traditionally higher rebate percentages becoming subject to generic competition and being replaced with sales of newer products with lower rebate percentages.

The total accruals for rebates, discounts, allowances and returns in the US pharmaceuticals business were as follows:

	At 31st December 2006 £m	At 31st December 2005 £m
Managed care, GPO rebates and Medicare, Part D	435	401
Chargebacks	50	56
US Government and State programmes	283	417
Cash discounts	24	27
Customer returns	184	146
Other	69	53
Total	1,045	1,100

Financial review 2006

continued

A monthly process is operated to monitor inventory levels at wholesalers for any abnormal movements. This process uses gross sales volumes, prescription volumes based on third party data sources and information received from key wholesalers. The aim of this is to maintain inventories at a consistent level from year to year based on the pattern of consumption. On this basis, US pharmaceutical inventory levels at wholesalers and in other distribution channels at 31st December 2006 were estimated to amount to approximately one month of turnover. This calculation uses third party information, the accuracy of which cannot be totally verified, but is believed to be sufficiently reliable for this purpose.

Taxation

Current tax is provided at the amounts expected to be paid, and deferred tax on temporary differences between the tax bases of assets and liabilities and their carrying amounts, at the rates that have been enacted or substantially enacted by the balance sheet date.

The Group has open tax issues with a number of revenue authorities, principally in relation to transfer pricing disputes. GSK uses the best advice in determining its transfer pricing methodology and in seeking to manage transfer pricing issues to a satisfactory conclusion and, on the basis of external professional advice, continues to believe that it has made adequate provision for the liabilities likely to arise from open assessments. However, there continues to be a wide difference of views where open issues exist. The ultimate liability for such matters may vary from the amounts provided and is dependent upon the outcome of litigation proceedings and negotiations with the relevant tax authorities.

Legal and other disputes

GSK provides for anticipated settlement costs where a reasonable estimate may be made of the likely outcome of the dispute and legal and other expenses arising from claims against the Group. The company's Directors, having taken legal advice, have established provisions after taking into account the relevant facts and circumstances of each matter and in accordance with accounting requirements. Provisions for product liability claims on certain products have been made on an 'incurred but not reported' basis where sufficient history of claims made and settlements is available. No provisions have been made for other unasserted claims or for claims for which no reasonable estimate of the likely outcome can yet be made. The ultimate liability for pending and unasserted claims may vary from the amounts provided, if any, and is dependent upon the outcome of litigation proceedings, investigations and possible settlement negotiations.

Impairment of fixed assets

The carrying values of fixed assets subject to depreciation and amortisation are reviewed for impairment when there is an indication that the values of the assets might be impaired. Impairment is determined by reference to the higher of net realisable value and value in use, measured by reference to risk-adjusted future cash flows discounted using appropriate interest rates. These future cash flows are based on business forecasts and are therefore inherently judgemental. Future events could cause the assumptions used in these impairment reviews to change with a consequent adverse effect on the future results of the Group.

Intangible assets

Where intangible assets are acquired by GlaxoSmithKline from third parties the costs of acquisition are capitalised. Licences to compounds in development are amortised from the point at which they are available for use, over their estimated useful lives, up to 20 years. Estimated useful lives are reviewed annually and impairment tests are undertaken if events occur which call into question the carrying values of the assets. Brands acquired with businesses are capitalised independently where they are separable and have an expected life of more than one year. Brands are amortised over their estimated useful lives, not exceeding 20 years, except where the end of the useful economic life cannot be foreseen. Where brands are not amortised, they are subject to annual impairment tests. Impairment tests are based on risk-adjusted future cash flows discounted using appropriate interest rates. These future cash flows are based on business forecasts and are therefore inherently judgemental. Future events could cause the values of these intangible assets to be impaired and this would have an adverse effect on the future results of the Group.

Pensions and other post-employment benefits

The costs of providing pensions and other post-retirement benefits are charged to the income statement in accordance with IAS 19 over the period during which benefit is derived from the employee's services. The costs are assessed in accordance with advice received from independent actuaries on the basis of assumptions selected by management for use under both IFRS and US GAAP. These assumptions include future earnings and pension increases, discount rates and expected long term rates of return on assets and are disclosed in Note 26 to the financial statements, 'Pensions and other post-employment benefits'. The expected long term rates of return on bonds are determined based on the portfolio mix of index-linked, government and corporate bonds. An equity risk premium is added to this for equities. Discount rates are based on appropriate long-term indices, including the iBoxx over 15 year AA index for the UK, and Moody's Aa index for the USA. Sensitivity analysis is provided in Note 26, but a 0.25% reduction in the discount rate would lead to an increase in the net pension deficit of approximately £369 million and an increase in the annual pension cost of approximately £4 million. The selection of different assumptions could affect the future results of the Group.

Product rights and goodwill

In addition to the critical accounting policies outlined above, the accounting policy for product rights and goodwill is deemed to be important in respect of the balance sheet prepared in accordance with US generally accepted accounting principles. Under US GAAP the merger of Glaxo Wellcome and SmithKline Beecham in 2000 was accounted for as an acquisition which gave rise to product rights of £24 billion and goodwill of £16 billion being recognised. Goodwill and those product rights determined to have indefinite lives are not amortised but rather reviewed annually for impairment. These impairment reviews assess business projections prepared as part of the Group's annual budgeting and planning process to determine whether or not an impairment in value has occurred. The business projections include assumptions about future events. Changes in future events could cause the assumptions in the business projections to change with a consequent adverse effect on the future results of the Group as reported under US GAAP.

Financial position and resources

Financial position

	2006 £m	2005 £m
Assets		
Non-current assets		
Property, plant and equipment	6,930	6,652
Goodwill	758	696
Other intangible assets	3,293	3,383
Investments in associates and joint ventures	295	276
Other investments	441	362
Deferred tax assets	2,123	2,214
Other non-current assets	721	438
Total non-current assets	14,561	14,021
Current assets		
Inventories	2,437	2,177
Current tax recoverable	186	416
Trade and other receivables	5,317	5,348
Liquid investments	1,035	1,025
Cash and cash equivalents	2,005	4,209
Assets held for sale	12	2
Total current assets	10,992	13,177
Total assets	25,553	27,198
Liabilities		
Current liabilities		
Short-term borrowings	(718)	(1,200)
Trade and other payables	(4,871)	(5,147)
Current tax payable	(621)	(2,269)
Short-term provisions	(1,055)	(895)
Total current liabilities	(7,265)	(9,511)
Non-current liabilities		
Long-term borrowings	(4,772)	(5,271)
Deferred tax provision	(595)	(569)
Pensions and other post-employment benefits	(2,339)	(3,069)
Other provisions	(528)	(741)
Other non-current liabilities	(406)	(467)
Total non-current liabilities	(8,640)	(10,117)
Total liabilities	(15,905)	(19,628)
Net assets	9,648	7,570
Equity		
Share capital	1,498	1,491
Share premium account	858	549
Retained earnings	6,965	5,579
Other reserves	65	(308)
Shareholders' equity	9,386	7,311
Minority interests	262	259
Total equity	9,648	7,570

Property, plant and equipment

The total cost of the Group's property, plant and equipment at 31st December 2006 was £13.3 billion, with a net book value of £6.9 billion. Of this, land and buildings represented £2.8 billion, plant and equipment £2.7 billion and assets in construction £1.4 billion. In 2006, GSK invested £1,485 million in new and renewal property, plant and equipment. This is mainly related to a large number of projects for the renewal improvement and expansion of facilities at various worldwide sites. Property is mainly held freehold. New investment is financed from Group liquid resources. At 31st December 2006, GSK had capital contractual commitments for future expenditure of some £521 million and 2007 operating lease commitments of £374 million.

GSK's business is science-based, technology-intensive and highly regulated by governmental authorities. The Group allocates significant financial resources to the renewal and maintenance of its property, plant and equipment to minimise risks of interruption of production and to achieve compliance with regulatory standards. A number of its processes use chemicals and hazardous materials.

The Group observes stringent procedures and uses specialist skills to manage environmental risks from these activities. Environmental issues, sometimes dating from operations now modified or discontinued, are reported under 'Responsibility for environment, health and safety' (page 24) and in Note 43 to the financial statements, 'Legal proceedings'. GSK believes that its facilities are adequate for its current needs.

Other intangible assets

Other intangible assets include the cost of intangibles acquired from third parties and computer software. The net book value of other intangible assets as at 31st December 2006 was £3,293 million (2005 – £3,383 million). The decrease in 2006 reflects currency movements and amortisation of existing intangibles, partly offset by additions of £444 million. The largest element of the additions relates to the acquisition of CNS, Inc. which added to the GSK portfolio *Breathe Right* nasal strips and *FiberChoice* dietary products.

Investments

GSK held investments, including associates and joint ventures, with a carrying value at 31st December 2006 of £736 million (2005 – £638 million). The market value at 31st December 2006 was £1,461 million (2005 – £1,487 million). The investments are mainly in equity shares where the holding derives directly from the Group's business. The largest of these investments is in the associate, Quest Diagnostics Inc., which had a book value at 31st December 2006 of £262 million (2005 – £244 million). The investments include stakes in companies where the Group has research collaborations, which provide access to biotechnology developments of potential interest or interests in companies that arise from business divestments.

Trade and other receivables

Trade and other receivables include £80 million (2005 – £180 million) of derivative financial instruments now held at fair value. The remaining increase from 2005 reflects increased sales and higher VAT recoverables partly offset by the impact of weakening overseas currencies on the translation of foreign currency receivables.

Trade and other payables

Trade and other payables include £41 million (2005 – £171 million) of derivative financial instruments now held at fair value. The remaining decrease reflects the impact of weakening overseas currencies on the translation of foreign currency payables.

Financial position and resources

continued

Provisions

The Group carried deferred tax provisions and other short-term and non-current provisions of £2,178 million at 31st December 2006 (2005 – £2,205 million) in respect of estimated future liabilities, of which £1,105 million related to legal and other disputes.

Provision has been made for legal and other disputes, indemnified disposal liabilities and the costs of manufacturing restructuring and merger integration to the extent that at the balance sheet date an actual or constructive obligation existed and could be reasonably estimated.

Pensions and other post-employment benefits

The Group accounts for pension and other post-employment arrangements in accordance with IAS 19. The net deficit before allowing for deferred taxation was £2,338 million (2005 – £3,069 million). The pension and other post-employment liabilities decreased following improvements in asset values, further special funding contributions to the UK and US pension funds of £346 million (2005 – £366 million) and a strengthening of long-term interest rates, including an increase in the rate used to discount UK pension liabilities from 4.75% to 5.0%.

Net debt

	2006 £m	2005 £m
Cash, cash equivalents and liquid investments	3,040	5,234
Borrowings – repayable within one year	(718)	(1,200)
Borrowings – repayable after one year	(4,772)	(5,271)
Net debt	(2,450)	(1,237)

Net debt increased by £1,213 million primarily due to the gross payment of \$3.3 billion (£1.8 billion) under the transfer pricing dispute settlement with the US Internal Revenue Service (see 'Taxation' on page 36) and higher share repurchases partly offset by increased operating profits.

Total equity

A summary of the movements in equity is set out below.

	2006 £m	2005 £m
Total equity at beginning of year	7,570	5,937
Implementation of accounting for financial instruments under IAS 39	–	(12)
Total equity at beginning of year, as adjusted	7,570	5,925
Total recognised income and expense for the year	5,395	4,576
Dividends to shareholders	(2,598)	(2,390)
Ordinary shares issued	316	252
Ordinary shares purchased and held as Treasury shares	(1,348)	(1,000)
Ordinary shares issued by ESOP Trusts	151	68
Share-based payments	247	265
Changes in minority interest shareholdings–	2	(40)
Minority interests	(87)	(86)
Total equity at end of year	9,648	7,570

At 31st December 2006, total equity had increased from £7,570 million at 31st December 2005 to £9,648 million. The increase arises principally from retained earnings and actuarial gains on defined benefit pension plans in the year, partially offset by further purchases of Treasury shares.

Share purchases

In 2006, the ESOP Trusts did not make any market purchases of shares in GSK plc (2005 – nil). Shares are held by the Trusts to satisfy future exercises of options and awards under the Group share option and award schemes. A proportion of the shares held by the Trusts are in respect of awards where the rules of the scheme require the company to satisfy exercises through market purchases rather than the issue of new shares. The shares held by the Trusts are matched to options and awards granted and diminish the dilutive effect of new share issues on shareholders' equity and earnings.

At 31st December 2006, the ESOP Trusts held 153.5 million GSK shares against the future exercise of share options and share awards. The carrying value of £1,999 million has been deducted from other reserves. The market value of these shares was £2,062 million.

GSK repurchased £1,348 million of shares in 2006, to be held as Treasury shares. The company completed its second £4 billion share repurchase programme in September, and in October commenced a new share buy-back programme totalling £6 billion. This programme is expected to be completed over a three year period including £2 billion in 2007. The exact amount and timing of future purchases, and the extent to which repurchased shares will be held as Treasury shares rather than being cancelled, will be determined by the company and is dependent on market conditions and other factors. At 31st December 2006, GSK also held 235.5 million shares as Treasury shares, at a cost of £3,147 million, which has been deducted from retained earnings.

Commitments and contingent liabilities

Financial commitments are summarised in Note 37 to the financial statements, 'Commitments'. Other contingent liabilities and obligations in respect of short and long-term debt are set out in Note 29 to the financial statements, 'Contingent liabilities' and Note 30 to the financial statements, 'Net debt'.

Amounts provided for pensions and post-retirement benefits are set out in Note 26 to the financial statements, 'Pensions and other post-employment benefits'. Amounts for restructuring and integration plans and legal, environmental and other disputes are set out in Note 27 to the financial statements, 'Other provisions'.

Contractual obligations and commitments

The following table sets out the Group's contractual obligations and commitments at 31st December 2006 as they fall due for payment.

	Total £m	Under 1 yr £m	1-3 yrs £m	3-5 yrs £m	5 yrs+ £m
Loans	5,351	676	1,505	11	3,159
Interest on loans	2,875	215	344	307	2,009
Finance lease obligations	139	42	63	22	12
Operating lease commitments	374	94	129	74	77
Intangible assets	3,219	558	465	645	1,551
Property, plant & equipment	521	381	140	–	–
Investments	196	192	4	–	–
Business combinations	258	258	–	–	–
Purchase commitments	299	151	128	20	–
Pensions	975	325	650	–	–
Theravance put option agreement	258	258	–	–	–
Other commitments	65	31	25	4	5
Total	14,530	3,181	3,453	1,083	6,813

Financial position and resources

continued

Commitments in respect of future interest payable on loans are disclosed after taking into account the effect of interest rate swaps.

The Group has entered into a number of research collaborations to develop new compounds with other pharmaceutical companies. The terms of these arrangements can include up-front fees, equity investments, loans and commitments to fund specified levels of research. In addition the Group will often agree to make further payments if future 'milestones' are achieved. As some of these agreements relate to compounds in the early stages of development, milestone payments will continue for a number of years if the compounds move successfully through the development process. Generally the closer the product is to marketing approval the greater the possibility of success. The payments shown above within intangible assets represent the maximum that would be paid if all milestones are achieved. A number of commitments were made in 2006 under licensing and other agreements, including with ChemoCentryx Inc., EPIX Pharmaceuticals Inc. and Genmab A/S.

In 2006, GSK formalised an agreement with the trustees of the UK pension schemes to make additional contributions of up to £325 million per year, in addition to the normal contributions, over a four-year period ending 31st December 2009 in order to eliminate the then pension deficits on an IAS 19 basis by that point. The table on page 40 shows this commitment, but excludes the normal ongoing annual funding requirement of approximately £200 million. GSK has also committed to eliminate any future deficits that may arise over a rolling five-year period. No other commitments have been made past 31st December 2009.

Contingent liabilities

The following table sets out contingent liabilities, comprising discounted bills, performance guarantees, letters of credit and other items arising in the normal course of business and when they are expected to expire.

	Total £m	Under 1 yr £m	1-3 yrs £m	3-5 yrs £m	5 yrs+ £m
Guarantees	221	74	28	5	114
Other contingent liabilities	37	12	10	4	11
Total	258	86	38	9	125

In the normal course of business GSK has provided various indemnification guarantees in respect of business disposals in which legal and other disputes have subsequently arisen. A provision is made where a reasonable estimate can be made of the likely outcome of the dispute and this is included in Note 27 to the financial statements, 'Other provisions'.

It is the Group's policy to provide for the settlement costs of asserted claims and environmental disputes when a reasonable estimate may be made. Prior to this point no liability is recorded. Legal and environmental costs are discussed in 'Risk factors' on pages 44 to 47.

GSK uses the best advice in determining its transfer pricing methodology and, on the basis of external professional advice, continues to believe that it has made adequate provision for the liabilities likely to arise from open taxation assessments. The ultimate liability for such matters may vary significantly from amounts provided and is dependent upon the outcome of litigation proceedings and negotiations with the relevant tax authorities. This is discussed further in Note 12 to the financial statements, 'Taxation'.

Cash flow

A summary of the consolidated cash flow statement is set out below:

	2006 £m	2005 £m
Net cash inflow from operating activities	4,357	5,958
Net cash outflow from investing activities	(1,521)	(1,660)
Net cash outflow from financing activities	(4,792)	(2,914)
Decrease/increase in cash and bank overdrafts	(1,956)	1,384
Exchange adjustments	(254)	233
Cash and bank overdrafts at beginning of year	3,972	2,355
Cash and bank overdrafts at end of year	1,762	3,972
Cash and bank overdrafts at end of year comprise:		
Cash and cash equivalents	2,005	4,209
Overdrafts	(243)	(237)
	1,762	3,972

The net cash inflow from operating activities after taxation paid was £4,357 million, a decrease of £1,601 million over 2005, arising mainly from the gross taxation payment of \$3.3 billion (£1.8 billion) under the transfer pricing dispute settlement (see page 36), partially offset by higher operating profits.

The net cash outflow from investing activities was £1,521 million, a decrease of £139 million which reflected increased capital expenditure and the purchase of businesses including CNS in 2006 for £273 million (purchases of businesses in 2005 were over £1 billion reflecting the purchase of Corixa and ID Biomedical).

Free cash flow was £2,623 million, a decrease of 44% over 2005, principally reflecting the US tax settlement and higher levels of capital expenditure. Free cash flow is the amount of cash generated by the business after meeting its obligations for interest, tax and dividends paid to minority interests, and after capital expenditure on non-current tangible and intangible assets.

Free cash flow is used by GSK's management for planning and reporting purposes and in discussions with and presentations to investment analysts and rating agencies. GSK's free cash flow measure is not defined in IFRS. This measure may not be directly comparable with similarly described measures used by other companies. A reconciliation of net cash inflow from operating activities, which is the closest equivalent IFRS measure, to free cash flow is shown below.

Reconciliation of free cash flow

	2006 £m	2005 £m
Net cash inflow from operating activities	4,357	5,958
Purchase of non-current tangible assets	(1,366)	(903)
Purchase of non-current intangible assets	(224)	(278)
Disposal of non-current tangible fixed assets	43	54
Interest paid	(414)	(381)
Interest received	299	290
Dividends received from joint ventures and associated undertaking	15	10
Dividends paid to minority interests	(87)	(86)
Free cash flow	2,623	4,664

Financial position and resources

continued

Reconciliation of net cash flow to movement in net debt

	2006 £m	2005 £m
Net debt at beginning of year	(1,237)	(1,984)
(Decrease)/increase in cash and bank overdrafts	(1,956)	1,384
Cash outflow/(inflow) from liquid investments	55	(550)
Net increase in long-term loans	-	(912)
Net repayment of short-term loans	739	857
Exchange and other movements	(51)	(32)
Net debt at end of year	(2,450)	(1,237)

Investment appraisal

GSK has a formal process for assessing potential investment proposals in order to ensure decisions are aligned with the Group's overall strategy. This process includes an analysis of the impact of the project on earnings, its return on invested capital and an assessment of the return based on discounted cash flows. The discount rate used to perform financial analysis is decided internally, to allow determination of the extent to which investments cover the Group's cost of capital. For specific investments the discount rate may be adjusted to take into account country or other risk weightings.

Capital expenditure and financial investment

Cash payments for tangible and intangible fixed assets amounted to £1,590 million (2005 – £1,181 million). Disposals realised £218 million (2005 – £275 million). Cash payments to acquire equity investments of £57 million (2005 – £23 million) were made in the year and sales of equity investments realised £32 million (2005 – £35 million).

Future cash flow

The Group expects that future operating cash flow will be sufficient to fund its operating and debt service costs, to satisfy normal levels of capital expenditure, to meet obligations under existing licensing agreements and to meet other routine outflows including tax and dividends, subject to the risk factors discussed on pages 44 to 47. GSK may from time to time have additional demands for finance, such as for acquisitions. It has access to other sources of liquidity from banks and other financial institutions, in addition to the cash flow from operations, for such needs.

Payment policies

Group companies are responsible for monitoring and managing their working capital. The terms of sales collections and supplier payments reflect local commercial practice.

In the UK, the company and each of its UK subsidiaries have policies to ensure that suppliers are paid on time. In particular, the UK companies seek:

- to settle terms of payment with suppliers when agreeing the terms of the transaction
- to ensure that suppliers are made aware of the agreed terms of payment
- to abide by the terms of payment.

The policy includes arrangements for accelerated payment of small suppliers.

Payment performance

At 31st December 2006, the average number of days' purchases represented by trade and fixed asset creditors of the parent company was nil (2005 – nil) and in respect of the company and its UK subsidiaries in aggregate was 24 days (2005 – 22 days).

Treasury policies

GlaxoSmithKline plc reports in Sterling and pays dividends out of sterling profits. The role of Corporate Treasury in GSK is to manage and monitor the Group's external and internal funding requirements and financial risks in support of Group corporate objectives. Treasury activities are governed by policies and procedures approved by the Board and monitored by a treasury management group.

GSK maintains treasury control systems and procedures to monitor foreign exchange, interest rate, liquidity, credit and other financial risks.

Liquidity

GSK operates globally, primarily through subsidiary companies established in the markets in which the Group trades. Due to the nature of GSK's business, with patent protection on many of the products in its portfolio, the Group's products compete largely on product efficacy rather than on price. Selling margins are sufficient to exceed normal operating costs and the Group's operating subsidiaries are substantially cash generative.

Operating cash flow is used to fund investment in the research and development of new products as well as routine outflows of capital expenditure, tax, dividends and repayment of maturing debt. The Group may, from time to time, have additional demands for finance, such as for share purchases and acquisitions.

GSK operates with a high level of interest cover and at low levels of net debt relative to its market capitalisation. In addition to the strong positive cash flow from normal trading activities, additional liquidity is readily available via its commercial paper programme and short-term investments. The Group also has a European Medium Term Note programme of £10 billion, of which £3.5 billion was in issue at 31st December 2006. In 2004, the Group established a US Shelf Registration of \$5 billion; at 31st December 2006 \$2.4 billion (£1.2 billion) was in issue.

Treasury operations

The objective of treasury activity is to manage the post-tax net cost/income of financial operations to the benefit of Group earnings. Corporate Treasury does not operate as a profit centre. GSK uses a variety of financial instruments, including derivatives, to finance its operations and to manage market risks from those operations.

Derivatives, principally comprising forward foreign currency contracts, interest rate and currency swaps, are used to swap borrowings and liquid assets into the currencies required for Group purposes and to manage exposure to funding risks from changes in foreign exchange rates and interest rates.

Financial position and resources

continued

GSK balances the use of borrowings and liquid assets having regard to the cash flow from operating activities, the currencies in which it is earned, the tax cost of intra-Group distributions, the currencies in which business assets are denominated, and the post-tax cost of borrowings compared with the post-tax return on liquid assets.

Liquid assets surplus to the immediate operating requirements of Group companies are generally invested and managed centrally by Corporate Treasury. Requirements of Group companies for operating finance are met whenever possible from central resources.

External borrowings, mainly managed centrally by Corporate Treasury, comprise a portfolio of long and medium-term instruments and short-term finance.

GSK does not hold or issue derivative financial instruments for trading purposes and the Group's Treasury policies specifically prohibit such activity. All transactions in financial instruments are undertaken to manage the risks arising from underlying business activities, not for speculation.

Funding, maturity and counterparty risk

The Group invests centrally managed liquid assets in government bonds, short-term corporate debt instruments with a minimum short-term credit rating of A-1/P-1, money market funds with a credit rating of AAA/Aaa and other structured investments (credit ratings shown are from Standard and Poor's and Moody's Investors' Services, respectively).

The Group manages its net borrowing requirements through a portfolio of long-term borrowings, including bonds, together with short-term finance under the US\$10 billion commercial paper programme.

The Group's long-term borrowings mature at dates between 2007 and 2034. These include a private financing which, although maturing in 2032, may be redeemed by GSK at any time and, in particular, in the event of any accelerating event that would increase the cost of funding for the Group. GSK's long-term debt rating is AA from Standard and Poor's and Aa2 from Moody's Investors' Services. The agencies' short-term ratings for paper issued under the Group's commercial paper programme are A-1+ and P-1 respectively.

Foreign exchange risk management

In GSK foreign currency transaction exposure arising on normal trade flows, in respect of both external and intra-Group trade, is not hedged. The policy is to minimise the exposure of overseas operating subsidiaries to transaction risk by matching local currency income with local currency costs. For this purpose, intra-Group trading transactions are matched centrally and intra-Group payment terms are managed to reduce risk. Exceptional foreign currency cash flows are hedged selectively under the management of Corporate Treasury.

The Group seeks to denominate borrowings in the currencies of its principal assets and cash flows. These are primarily denominated in US dollars, Euros and Sterling. Certain of these and other borrowings are swapped into other currencies as required for Group purposes.

Borrowings denominated in, or swapped into, foreign currencies that match investments in overseas Group assets are treated as a hedge against the relevant net assets.

Based on the composition of net debt at 31st December 2006, a 10% appreciation in Sterling against major currencies would result in a reduction in the Group's net debt of approximately £210 million. A 10% weakening in Sterling against major currencies would result in an increase in the Group's net debt of approximately £256 million.

Interest rate risk management

GSK's policy on interest rate risk management requires that the amount of net borrowings at fixed rates increases with the ratio of forecast net interest payable to trading profit.

The Group uses a limited number of interest rate swaps to redenominate external borrowings into the interest rate coupon required for Group purposes. The duration of these swaps matches the duration of the principal debt instruments. Interest rate derivative instruments are accounted for as fair value or cash flow hedges of the relevant assets or liabilities.

The Group manages centrally the short-term cash surpluses or borrowing requirements of subsidiary companies and uses forward contracts to hedge future repayments back into the originating currency.

Sensitivity analysis considers the sensitivity of the Group's net debt to hypothetical changes in market rates and assumes that all other variables remain constant. Based on the composition of net debt and financing arrangements at 31st December 2006, and taking into consideration all fixed rate borrowings in place, a one percentage point (100 basis points) decrease in average interest rates would result in an increase in the Group's annual net interest charge of approximately £5 million.

Equity risk management

Equity investments classified as current assets are available-for-sale and the Group manages disposals to meet overall business requirements as they arise. The Group regularly monitors the value of its equity investments and only enters into hedges selectively with the approval of the Board.

Financial assets and liabilities

An analysis of net debt is given in Note 30 to the financial statements, 'Net debt'. An analysis of financial assets and liabilities at carrying value and fair value and a reconciliation to net debt are given in Note 39 to the financial statements, 'Financial instruments and related disclosures', together with a discussion of derivative financial instruments and quantitative disclosures about market risk in accordance with the requirements of IAS 32 and IAS 39.

The Group continues to benefit from strong positive cash flow. Group net debt would have decreased significantly in the year to 31st December 2006, but for the Group's purchase of its own shares in the market of £1.3 billion, the gross US tax settlement of US\$3.3 billion (£1.8 billion) and acquisitions of approximately £0.3 billion.

The financial assets and liabilities at 31st December 2006 are representative of the treasury policies and strategies of GSK, applied consistently during the year. There were no significant changes in such policies throughout the year.

Outlook and risk factors

Outlook

Sales growth of existing products and launch of new products are key drivers of GSK's business performance. The sales growth seen from key products such as *Seretide/Advair*, the *Avandia* group of products, Vaccines, *Lamictal*, *Valtrex*, *Coreg* and the high potential products, *Requip*, *Avodart* and *Boniva* is expected to continue in 2007.

Typically, sales of existing products decline dramatically when generic competition is introduced either on patent expiry or earlier if there is a successful challenge to the Group's patent. In Q4 2006, generic competitors to *Wellbutrin XL* 300mg tablet (approximately 60% of *Wellbutrin* sales) and *Zofran* entered the US market. GSK is engaged in legal proceedings regarding the validity and infringement of the Group's patents relating to many of its products. These are discussed in 'Risk factors' below and in Note 43 to the financial statements, 'Legal proceedings'.

Five major new pharmaceutical product launches are expected in 2007. These include *Tykerb*, for breast cancer, *Cervarix*, for cervical cancer (in Europe), *Allermist*, for allergic rhinitis, *Coreg CR*, for heart failure and *Trexima*, for migraine.

GSK also expects to launch several other important products during the year including: *Arixtra*, to treat acute coronary syndromes (ACS); *Altanax/Altargo*, for skin infections, and *Entereg*, for the management of post-operative ileus.

GSK's consumer brand portfolio will be strengthened further in 2007, with the launch of 10 products, including *alli*, a new treatment for weight-loss in the USA. Two more brands, *Breathe Right*, nasal strips and *FiberChoice*, dietary fibre supplements, were added to the portfolio, following the acquisition of CNS, Inc. which was completed in December 2006.

Several new products are expected to be filed for approval with the regulatory authorities in 2007, including vaccine opportunities: US filing of *Cervarix*, for cervical cancer and *Rotarix*, for rotavirus and the European filing of *Synflorix*, a vaccine for pneumococcal disease. GSK continues to progress development of vaccines for use before, and in the event of, a 'flu pandemic. In January 2007, GSK submitted its H5N1 vaccine to European regulators for approval for pre-pandemic use.

GSK now has 31 major product opportunities in phase III development or registration, comprising 13 NCEs, 6 new vaccines and 12 product line extensions.

GSK's published earnings guidance for 2007 is that earnings per share growth is expected to be 8% to 10% in CER terms.

The Group has net debt of £2.5 billion, which is low relative to its market capitalisation, and this positions it to take advantage of any opportunities that might arise to build the business.

There are risks and uncertainties inherent in the business that may affect future performance including R&D projects, anticipated sales growth and expected earnings growth. These are discussed in 'Risk factors' below.

Risk factors

There are risks and uncertainties relevant to the Group's business. The factors listed below are among those that the Group thinks could cause the Group's actual results to differ materially from expected and historical results.

Risk that R&D will not deliver commercially successful new products

Continued development of commercially viable new products is critical to the Group's ability to replace sales of older products that decline upon expiration of exclusive rights, and to increase overall sales. Developing new products is a costly, lengthy and uncertain process.

A new product candidate can fail at any stage of the process, and one or more late-stage product candidates could fail to receive regulatory approval.

New product candidates may appear promising in development but, after significant investment, fail to reach the market or have only limited commercial success. This, for example, could be as a result of efficacy or safety concerns, inability to obtain necessary regulatory approvals, difficulty or excessive costs to manufacture, erosion of patent term as a result of a lengthy development period, infringement of patents or other intellectual property rights of others or inability to differentiate the product adequately from those with which it competes.

Risk of unplanned loss of patents

Patent infringement litigation

The Group's patents, in common with all patents, can be challenged at any time. Efforts by generic manufacturers may involve challenges to the validity of a patent or assertions that their generic product does not infringe the Group's patents. If the Group is not successful in defending an attack on its patents and maintaining exclusive rights to market one or more of its major products, particularly in the USA where the Group has its highest turnover and margins, the Group's turnover and margins would be adversely affected. See Note 43 to the financial statements, 'Legal proceedings', for a discussion of patent-related proceedings in which the Group is involved.

Generic drug manufacturers are seeking to market generic versions of many of the Group's most important products, prior to the expiration of the Group's patents, and have exhibited a readiness to do so for other products in the future. The US launch of generic products competing with *Paxil IR* and *Wellbutrin* had a significant impact on the Group's overall turnover and earnings.

Weakness of intellectual property protection in certain countries

In some of the countries in which the Group operates, patent protection may be significantly weaker than in the USA or the European Union. In addition, in an effort to control public health crises, some developing countries, such as South Africa and Brazil, have considered plans for substantial reductions in the scope of patent protection for pharmaceutical products. In particular, these countries could facilitate competition within their markets from generic manufacturers who would otherwise be unable to introduce competing products for a number of years.

Any loss of patent protection, including abrogation of patent rights or compulsory licensing, is likely to affect adversely the Group's operating results in those national markets but is not expected to be material to the Group overall. Absence of adequate patent protection could limit the opportunity to look to such markets for future sales growth.

Risk of substantial adverse outcome of litigation and government investigations

See Note 43 to the financial statements, 'Legal proceedings', for a discussion of proceedings and governmental investigations in which the Group is currently involved. Unfavourable resolution of these and similar future proceedings or investigations may have a material adverse effect on the Group's financial results. The Group has made material provisions in 2004, 2005 and 2006 related to legal proceedings and investigations which reduced its earnings. The Group may also make additional significant provisions related to legal proceedings and investigations in the future, which would reduce its earnings. In many cases the practice of the plaintiff bar is to claim damages – compensatory, punitive and statutory – in amounts that bear no relationship to the underlying harm. Accordingly it is potentially misleading to quantify the potential exposure to claims, proceedings and investigations of the type described in Note 43.

Recent insurance loss experience, including pharmaceutical product liability exposures, has increased the cost of, and narrowed the coverage afforded by, insurance for pharmaceutical companies generally, including the Group.

In order to contain insurance costs in recent years the Group has continued to adjust its coverage profile, accepting a greater degree of un-insured exposure. In addition, where claims are made under insurance policies, insurers may reserve the right to deny coverage on various grounds. If denial of coverage is ultimately upheld on these claims, this could result in material additional charges to the Group's earnings.

Product liability litigation

Pre-clinical and clinical trials are conducted during the development of potential products to determine the safety and efficacy of products for use by humans following approval by regulatory bodies. Notwithstanding these efforts, when drugs and vaccines are introduced into the marketplace, unanticipated side effects may become evident. The Group is currently a defendant in a number of product liability lawsuits, including class actions, that involve substantial claims for damages related to the Group's pharmaceutical products. Litigation, particularly in the USA, is inherently unpredictable and excessive verdicts that are not justified by the evidence can occur. Class actions that sweep together all persons who were prescribed the Group's products can inflate the potential liability by the force of numbers. Claims for pain and suffering and punitive damages are frequently asserted in product liability actions and, if allowed, can represent potentially open-ended exposure.

Anti-trust litigation

In the USA it has become increasingly common that following publicity around government investigations or an adverse outcome in prosecution of patent infringement actions, the defendants and direct and indirect purchasers and other payers initiate anti-trust actions as well. Claims by direct and indirect purchasers and other payers are typically filed as class actions and the relief sought may include treble damages and restitution claims. Damages in adverse anti-trust verdicts are subject to automatic trebling in the USA. Similarly, anti-trust claims may be brought following settlement of patent litigation, alleging that such settlements are anti-competitive and in violation of anti-trust laws.

Sales, marketing and regulation

The Group operates globally in complex legal and regulatory environments that often vary among jurisdictions. The failure to comply with applicable laws, rules and regulations in these jurisdictions may result in civil and criminal legal proceedings. As those rules and regulations change or as governmental interpretation of those rules and regulations evolve, prior conduct may be called into question. In the USA, for example, the Group is responding to federal and state governmental investigations into pricing, marketing and reimbursement of its prescription drug products. These investigations could result in related restitution or civil false claims act litigation on behalf of the federal or state governments, as well as related proceedings initiated against the Group by or on behalf of consumers and private payers. Such proceedings may result in trebling of damages awarded or fines in respect of each violation of law. Criminal proceedings may also be initiated against Group companies or individuals.

Risks of competition, price controls and limitations on sales

Third party competition

The Group operates in highly competitive businesses. In the pharmaceuticals business, it faces competition both from proprietary products of large international manufacturers and producers of generic pharmaceuticals. Significant product innovations, technical advances or the intensification of price competition by competitors could adversely affect the Group's operating results. Continued consolidation in the pharmaceutical industry could adversely affect the Group's competitive position, while continued consolidation among the Group's customers may increase pricing pressures. The Group had 13 products with over £500 million in annual global sales in 2006.

Among these products is *Augmentin IR*, with respect to which the Group has generic competition, and *Avandia*, *Valtrex*, and *Wellbutrin XL*, with respect to which the Group's intellectual property rights in the USA are currently the subject of litigation, and two others – *Zofran* and the 300 mg tablet version of *Wellbutrin XL* – with respect to which the Group has had generic competition since the fourth quarter of 2006.

Outlook and risk factors

continued

If these or any of the Group's other major products were to become subject to a problem such as unplanned loss of patent protection, unexpected side effects, regulatory proceedings, publicity affecting doctor or patient confidence or pressure from competitive products, or if a new, more effective treatment should be introduced, the adverse impact on the Group's revenues and operating results could be significant. In particular, the Group faces intense competition from manufacturers of generic pharmaceutical products in all of its major markets. Generic products often enter the market upon expiration of patents or data exclusivity periods for the Group's products. Introduction of generic products typically leads to a dramatic loss of sales and reduces the Group's revenues and margins for its proprietary products. The expiration dates for patents for the Group's major products are set out on page 23 and legal proceedings involving patent challenges are set out in Note 43 to the financial statements, 'Legal proceedings'.

Governmental and payer controls

Pharmaceutical products are subject to price controls or pressures and other restrictions in many markets, including Japan, Germany, France and Italy. Some governments intervene directly in setting prices. In addition, in some markets major purchasers of pharmaceutical products (whether governmental agencies or private health care providers) have the economic power to exert substantial pressure on prices or the terms of access to formularies.

The Group cannot predict whether existing controls will increase or new controls will be introduced that will reduce the Group's margins or affect adversely its ability to introduce new products profitably.

For example, in the USA, where the Group has its highest margins and most sales for any country, pricing pressures could significantly increase following implementation of the pharmaceutical benefit under Medicare or in the event that other state programmes to control the cost of prescription drugs are adopted. As experience develops under the Medicare programme outpatient pharmaceutical coverage for its beneficiaries that began in 2006, the US government, or the private insurers through which coverage is offered, through their enormous purchasing power under the programme could demand discounts that may implicitly create price controls on prescription drugs. Changes to the enabling legislation could afford the US government a direct role in negotiating prices under the Medicare programme. Additionally a number of states have proposed or implemented various schemes to control prices for their own senior citizens' programmes, including importation from other countries and bulk purchases of drugs. The growth in the number of patients covered through large managed care institutions in the USA, which is likely to increase with implementation of the Medicare benefit, also increases pricing pressures on the Group's products. These trends may adversely affect the Group's revenues and margins from sales in the USA.

Regulatory controls

The Group must comply with a broad range of regulatory controls on the testing, approval, manufacturing and marketing of many of its pharmaceutical and consumer healthcare products, particularly in the USA and countries of the European Union, that affect not only the cost of product development but also the time required to reach the market and the uncertainty of successfully doing so. Stricter regulatory controls also heighten the risk of withdrawal by regulators on the basis of post-approval concerns over product safety, which would reduce revenues and can result in product recalls and product liability lawsuits.

In addition, in some cases the Group may voluntarily cease marketing a product (for example, the withdrawal of *Lotronex* in 2000 shortly after its initial launch in the USA) or face declining sales based on concerns about efficacy or safety, whether or not scientifically justified, even in the absence of regulatory action. The development of the post-approval adverse event profile for a product or the product class may have a major impact on the marketing and sale of the product.

Risk of interruption of product supply

The manufacture of pharmaceutical products and their constituent materials requires compliance with good manufacturing practice regulations. The Group's manufacturing sites are subject to review and approval by the FDA and other regulatory agencies. Compliance failure by suppliers of key materials or the Group's own manufacturing facilities could lead to product recalls and seizures, interruption of production and delays in the approvals of new products pending resolution of manufacturing issues. Non-compliance can also result in fines and disgorgement of profits. Any interruption of supply or fines or disgorgement remedy could materially and adversely affect the Group's financial results. The Group's Cidra, Puerto Rico facility has worked at resolution of FDA observations of deficiencies in manufacturing practices and is subject to a consent decree entered into with the FDA during 2005, as referred to in Note 43 to the financial statements, 'Legal proceedings'. As a consequence of those discussions, supplies of certain products manufactured at Cidra were curtailed or constricted which had an adverse impact on sales in 2005 and 2006.

Although the Group undertakes business continuity planning, single sourcing for certain components, bulk active materials and finished products creates a risk of failure of supply in the event of regulatory non-compliance or physical disruption at the manufacturing sites.

Risk from concentration of sales to wholesalers

In the USA, in line with other pharmaceutical companies, the Group sells its products through a small number of wholesalers in addition to hospitals, pharmacies, physicians and other groups. Sales to the three largest wholesalers amounted to approximately 80% of the Group's US pharmaceutical sales. At 31st December 2006 the Group had trade receivables due from these three wholesalers totalling £1,044 million (31st December 2005 – £1,051 million). The Group is exposed to a concentration of credit risk in respect of these wholesalers such that, if one or more of them is affected by financial difficulty, it could materially and adversely affect the Group's financial results.

Reliance on information technology

The Group is increasingly dependent on information technology systems, including Internet-based systems, for internal communication as well as communication with customers and suppliers. Any significant disruption of these systems, whether due to computer viruses or other outside incursions, could materially and adversely affect the Group's operations.

Taxation

The effective tax rate on the Group's earnings benefits from the fact that a portion of its earnings is taxed at more favourable rates in some jurisdictions outside the UK. Changes in tax laws or in their application with respect to matters such as transfer pricing and the risk of double taxation that relate to the portion of the Group's earnings taxed at more favourable rates, or a restriction in tax relief allowed on the interest on intra-Group debt, could increase the Group's effective tax rate and adversely affect its financial results. In 2006 the Group resolved the claims by the US Internal Revenue Service related to Glaxo heritage products. The Group has open issues with the revenue authorities in the UK, Japan and Canada. These matters are discussed in Note 12 to the financial statements, 'Taxation'.

Disruption from pandemic influenza

In the event of pandemic influenza, the Group could be subject to disruption from a range of factors. National governments may be more willing to abrogate intellectual property rights for medicines that might otherwise be in short supply. In a country afflicted by pandemic 'flu, there would be a risk that employees and their families will be affected with the consequence that sales and distribution and manufacturing activities could be shut down and supply continuity – for active ingredients and finished goods – affected.

Environmental liabilities

The environmental laws of various jurisdictions impose actual and potential obligations on the Group to remediate contaminated sites. The Group has also been identified as a potentially responsible party under the US Comprehensive Environmental Response Compensation and Liability Act at a number of sites for remediation costs relating to the Group's use or ownership of such sites. Failure to manage properly the environmental risks could result in additional remedial costs that could materially and adversely affect the Group's operations. See Note 43 to the financial statements, 'Legal proceedings', for a discussion of environmental-related proceedings in which the Group is involved.

Global political and economic conditions

The Group conducts a substantial portion of its operations outside the UK. The Group's management of foreign exchange rates is discussed in Business Review, 'Foreign exchange risk management' (see page 43). Fluctuations in exchange rates between Sterling and other currencies, especially the US dollar, the Euro and the Japanese Yen, could materially affect the Group's financial results.

The Group has no control over changes in inflation and interest rates, foreign currency exchange rates and controls or other economic factors affecting its businesses or the possibility of political unrest, legal and regulatory changes or nationalisation in jurisdictions in which the Group operates. These factors could materially affect the Group's future results of operations.

Accounting standards

New or revised accounting standards, rules and interpretations promulgated from time to time by international or US accounting standard setting boards could result in changes to the recognition of income and expense that may adversely impact the Group's reported financial results. International and US accounting standards changes in the market valuation of certain financial instruments (such as the equity collar linked to the Group's investment in Quest Diagnostics, the put and call options linked to the Group's strategic alliance with Theravance and impairments of equity investments) are reflected in the Group's reported results before those gains or losses are actually realised and could have a significant impact on the income statement in any given period. Also, under international accounting standards, accounting for deferred taxation on inter-company inventory may give rise to volatility depending upon the ownership of the inventory at the balance sheet date.

Regulators regularly review the financial statements of listed companies like GSK for compliance with accounting and regulatory requirements.

The Group believes that it complies with the appropriate regulatory requirements concerning its financial statements and disclosures. However, other companies have experienced investigations into potential non-compliance with accounting and disclosure requirements that have resulted in restatements of previously reported results and sometimes significant penalties.

Human resources

The Group has approximately 100,000 employees around the world and is subject to laws and regulations concerning its employees – ranging from discrimination and harassment to personal privacy to labour relations – that vary significantly from jurisdiction to jurisdiction. Failure to continue to recruit and retain the right people and maintain a culture of compliance could have a significant adverse effect on the Group.

Financial review 2005

In accordance with US SEC disclosure requirements, the following discussion compares results for the year to 31st December 2005 with the results for the year to 31st December 2004. The information has been prepared under IFRS.

All growth rates are at constant exchange rates (CER) unless otherwise stated. The sterling growth rates may be found in the tables of pharmaceutical turnover by therapeutic area on page 50.

Exchange

The currencies that most influence the Group's results are the US dollar, the Euro and the Japanese Yen.

In 2005, the US dollar strengthened by over 10% against the pound, rising to \$1.72 at the year-end following two years of weakness. Both the Euro and Japanese Yen year-end rates weakened against the pound by just over 3%.

World market – pharmaceuticals

Global pharmaceutical sales increased by 6% in 2005 to £302 billion.

World market by geographic region	Value £bn	% of total	Growth £%
USA	132.0	44	3
Europe	86.8	29	8
Germany	16.4	5	8
France	15.9	5	9
UK	10.5	3	–
Italy	9.9	3	3
Japan	32.5	11	4
Asia Pacific	20.5	7	13
Latin America	13.7	4	15
Middle East, Africa	9.8	3	17
Canada	7.0	2	14
Total	302.3	100	6

Growth in the US market has slowed to 3%, but it still represents 44% of the global prescription pharmaceutical market compared with 30% a decade ago.

At 30th September 2005, GSK held second position in the world pharmaceutical market with a market share of 6.3%, behind Pfizer with a market share of 8.9%. GSK had eight of the world's top 60 pharmaceutical products. These were *Avandia*, *Flixonase*, *Imigran/Imitrex*, *Lamictal*, *Seretide/Advair*, *Seroxat/Paxil*, *Wellbutrin* and *Zofran*.

World market – top five therapeutic classes	Value £bn	% of total	CER%	Growth £%
Cardiovascular	50.7	17	7	6
Central nervous system	49.7	16	6	4
Alimentary tract and metabolic	36.6	12	6	5
Anti-infectives (bacterial, viral and fungal) excluding vaccines	32.2	11	7	5
Respiratory	20.7	7	8	7

(Note: data based on 12 months to 30th September 2005.)

Pharmaceutical turnover

Total pharmaceutical turnover in 2005 was £18,661 million compared with £17,100 million in 2004, an increase of 8% CER. In sterling terms turnover increased 9%, principally due to the strength of the Euro and other International currencies.

Pharmaceutical turnover by therapeutic area

GSK's ability to continue to deliver pharmaceutical turnover growth is primarily due to an exceptionally broad product portfolio of fast-growing, high-value products. Sales of GSK's largest product, *Seretide/Advair*, were up 22% to £3.0 billion and continued to gain market share across all regions. Market share by value in the anti-asthma and COPD therapy class was 27% in Europe and 33% in the USA, an increase of 2 percentage points in both cases compared with 2004. Sales of diabetes treatments were also strong, with *Avandia/Avandamet* up 18% to £1.3 billion. GSK launched *Avandia* for the treatment of type 2 diabetes in 1999 and a combination product, *Avandamet*, for blood sugar control in 2002. The product group was expanded further in February 2006 with the launch in the USA of a fixed-dose combination treatment, *Avandaryl*, which combines *Avandia* with a sulfonylurea. In 2005, *Avandia/Avandamet* achieved a market share by value in oral anti-diabetics of 14% in Europe and 35% in the USA, up 3 and 6 percentage points, respectively.

Other fast growing products were *Lamictal* for epilepsy/bipolar disorder, up 24% (£0.8 billion), *Valtrex* for herpes, up 21% (£0.7 billion), *Coreg* for heart disease, up 32% (£0.6 billion) and vaccines, up 15% (£1.4 billion).

In addition, in 2005 there was a rapid uptake of a number of high potential products such as *Requip*, for restless legs syndrome (sales up 34% to £156 million), *Avodart* for benign prostatic hyperplasia (sales doubled to £129 million) and *Boniva/Bonviva* for the treatment of osteoporosis, which was launched in 2005 and captured a 10% share of new prescriptions for oral bisphosphonates in the US market.

Respiratory

GSK continues to be the global leader in respiratory pharmaceuticals with sales of its three key products, *Seretide/Advair*, *Flixotide/Flovent* and *Serevent*, amounting to £4.0 billion, up 15%. *Seretide/Advair* sales rose 26% to £1.7 billion in the USA. Sales were also strong in both European and International markets, which were up 16% to £1 billion and £0.3 billion, respectively.

Central nervous system (CNS)

CNS sales declined 8% to £3.2 billion. Sales declined in the USA and Europe, with a small gain in International. Total *Paxil* sales fell 42% to £615 million, due to generic competition and the interruption in supply to *Paxil CR* during the year. See 'Product supply' on page 49. Partially mitigating this decline was the strong performance of *Paxil* in Japan, up 17% to £197 million.

Total *Wellbutrin* turnover fell 2% to £739 million. *Wellbutrin IR* and *SR* sales fell 68% to £92 million due to generic competition, but this was largely offset by the very strong performance of *Wellbutrin XL* (up 38% to £647 million).

The strong growth of GSK's epilepsy and bi-polar disorder treatment *Lamictal* continued, with sales up 24% to £849 million, driven by the indication for the maintenance treatment of bi-polar disorder.

Requip sales rose 34% to £156 million. By Q1 2006, weekly new prescriptions for the product have quadrupled in the USA since it was launched for restless legs syndrome (RLS) in Q2 2005.

Anti-virals

Global HIV product sales grew 5% to £1.6 billion, with sales from new products *Epzicom/Kivexa* and *Lexiva* (together more than doubling to £226 million) offsetting the performance of *Trizivir* (down 6% to £303 million) and *Epivir* (down 12% to £261 million). Sales of the herpes treatment *Valtrex* grew 21% to £695 million. Performance is being driven by the USA (up 26% to £470 million) where the product is the clear market leader in treatments for genital herpes.

Anti-bacterials

Anti-bacterial sales declined 3% worldwide. In the USA the decline was 27% reflecting increased generic competition.

Metabolic

The diabetes treatments *Avandia/Avandamet* continued to perform very strongly, with overall sales of £1.3 billion, up 18%. In the USA, sales grew 14% to £977 million. *Avandia/Avandamet* are also establishing strong positions in Europe, with sales rising 52% to £157 million, helped by the launch of *Avandamet*. Sales in International markets rose 13% to £195 million.

Boniva/Bonviva, a new once-monthly oral bisphosphonate for the treatment of osteoporosis, which was developed with Roche, had a strong launch in the USA and in February 2006 had a 10% share of new prescriptions for oral bisphosphonates. *Boniva* injection, the first-ever quarterly treatment for osteoporosis, was approved in the USA in January 2006 and received a positive opinion from the CHMP in Europe on 27th January 2006.

Vaccines

The vaccines business performed well, with total sales rising 15% to £1.4 billion, led by *Infanrix*. Vaccine sales were particularly strong in the USA, where turnover rose 26% to £338 million, helped by the launch of two new products, *Fluarix* and *Boostrix*.

In July, GSK acquired Corixa Corporation for £150 million and in December, completed the acquisition of ID Biomedical Corporation for £0.9 billion.

Oncology and emesis

Sales of *Zofran* grew 9% to £837 million, driven by the US market, up 12% to £639 million.

Cardiovascular and urogenital

Sales of *Coreg* for heart disease grew 32% to £573 million.

Avodart for benign prostatic hyperplasia (enlarged prostate) had a very strong year, with sales doubling to £129 million. By January 2006 the product accounted for 42% of new prescriptions in the US 5-Alpha Reductase Inhibitor market.

Other therapeutic areas

Sales of *Zantac* fell 12% to £244 million, with declines in all regions.

Product supply

Following FDA inspections in October 2003 and November 2004, which identified possible deficiencies in manufacturing practices at the Group's facility at Cidra in Puerto Rico, the FDA halted distribution of supplies of *Paxil CR* and *Avandamet* in March 2005. This site is engaged in tableting and packaging for a range of GSK products, primarily for the US market including *Paxil*, *Paxil CR*, *Coreg*, *Avandia* and *Avandamet*. In April 2005, the Group reached agreement with the FDA on a Consent Decree, which provides for an independent expert to review manufacturing processes at the site for compliance with FDA Good Manufacturing Practice requirements. The Decree also allows for potential future penalties, up to a maximum of \$10 million a year, if GSK fails to meet its terms.

In June 2005, the Group began re-supplying the US and other markets with both *Paxil CR* and *Avandamet*. The sales of these products were significantly impacted in 2005 by this interruption in supply. The impact on *Avandamet* was mitigated by the switching of patients to *Avandia*. In 2005, the Group also established a provision for the external costs required to rectify the manufacturing issues at the plant. For further details see Risk factors on pages 44 to 47 and Note 43 to the financial statements, 'Legal proceedings'.

Consumer Healthcare sales

	2005 £m	2004 £m	Growth	
			CER%	£%
OTC medicines	1,437	1,400	1	3
Analgesics	362	333	6	9
Dermatological	161	180	(12)	(11)
Gastro-intestinal	249	241	1	3
Respiratory tract	154	145	5	6
Smoking control	336	327	2	3
Natural wellness support	133	136	(4)	(2)
Oral care	943	913	2	3
Nutritional healthcare	619	573	7	8
	2,999	2,886	2	4

The growth in Consumer Healthcare sales of 2% to £3.0 billion comprised an OTC medicines sales increase of 1%, a Nutritional healthcare sales increase of 7% and an Oral care sales increase of 2%.

OTC medicines

Over-the-counter medicine sales were £1,437 million, up 1%. Growth from analgesics, up 6%, and respiratory tract, up 5%, helped offset the loss of sales from the dermatological products divested in 2004. *Panadol* growth of 12% in International markets was the key driver of the growth in analgesics.

Oral care

Oral care sales grew 2% to £943 million. Sales of *Sensodyne* and the denture care brands (*Polident*, *Poligrip* and *Corega*) grew by 12% and 6%, respectively, helping to offset lower sales of other toothpaste products.

Nutritional healthcare

Nutritional healthcare product sales grew 7% to £619 million. *Lucozade*, up 11%, continued to grow strongly in Europe.

Operating profit

The analysis below of operating profit and subsequent discussion compares the 2005 results with 2004 results.

	2005		2004		Growth	
	£m	%	£m	%	CER%	£%
Turnover	21,660	100.0	19,986	100.0	7	8
Cost of sales	(4,764)	(22.0)	(4,360)	(21.8)	8	9
Selling, general and administration	(7,250)	(33.5)	(7,201)	(36.0)	–	1
Research and development	(3,136)	(14.5)	(2,904)	(14.5)	8	8
Other operating income	364	1.7	235	1.1		
Operating profit	6,874	31.7	5,756	28.8	16	19

Cost of sales

Cost of sales as a percentage of turnover increased 0.2 percentage points. At constant exchange rates, the increase was also 0.2 percentage points, reflecting higher costs related to the ongoing rectification of manufacturing issues at the Cidra site in Puerto Rico, which were only partly offset by operating efficiencies compared with the previous year.

Selling, general and administration

Selling, general and administration (SG&A) as a percentage of turnover decreased 2.5 percentage points. At constant exchange rates, the decrease was 2.2 percentage points, reflecting flat expenditure compared with the prior year on a turnover increase of 7%. SG&A costs were in line with 2004 overall, with higher advertising, promotion and selling expense being offset by lower general and administration expenditure. Advertising, promotion and selling expenses increased 3% and accounted for a 2% increase in total SG&A. General and administration costs declined 4% and accounted for a 2% reduction in total SG&A.

This was due to lower charges related to legal matters, equal to a 2% reduction in total SG&A, and lower share-based payment charges, equal to a 1% decrease in total SG&A, partly offset by higher costs related to programmes to deliver future cost savings equal to a 1% increase in total SG&A.

Research and development

R&D expenditure as a percentage of turnover was 14.5%, in line with 2004, and increased 8% compared with the previous year, partly as a result of some write-offs of intangible assets. Excluding these write-offs, R&D expenditure grew slightly below turnover growth. Pharmaceuticals R&D expenditure represented 16.2% of pharmaceutical turnover.

Other operating income

Other operating income includes royalty income, equity investment disposals and impairments, product disposals and fair value adjustments to the Quest collar and Theravance options. Other operating income was £364 million in 2005 compared with £235 million in 2004. The increased income in 2005 is predominantly due to increased product and asset disposal gains compared with 2004, and a favourable fair value movement of £19 million in the Quest collar and the Theravance options.

Operating profit

Overall, the operating profit margin increased 2.9 percentage points as operating profit of £6,874 million increased 19% in sterling terms. At constant exchange rates operating profit increased 16% and the margin increased 2.5 percentage points, reflecting the lower charges relating to legal matters and share-based payments, higher product and asset disposals and increases in advertising, promotion and selling that were below the rate of turnover growth. Partially offsetting these items were higher costs related to programmes to deliver future cost savings and increased R&D expenditure.

Profit before taxation

The discussion below compares the 2005 results with the 2004 results. Gains from asset disposals, including associates, were £290 million (2004 – £295 million), costs for legal matters were £430 million (2004 – £595 million) and charges relating to cost-saving programmes were £141 million (2004 – £104 million). Share-based payments in 2005 were £236 million (2004 – £333 million).

Share of profits/(losses) of joint ventures and associated undertakings

The share of profits of associates arises principally from the Group's holding in Quest Diagnostics Inc..

Disposal of interest in associates

There were no disposals of interests in associates in 2005. During 2004, the Group disposed of 3.8 million shares from its investment in Quest Diagnostics Inc. for cash proceeds of £188 million. A profit of £150 million was recognised. The Group's shareholding in Quest as at 31st December 2005 was 18.4%.

Financial review 2005

continued

Net finance costs

	2005 £m	2004 £m
Finance income		
Interest income	276	173
Unwinding of discount on assets	–	3
Fair value adjustments	(19)	–
	257	176
Finance costs		
Interest costs	(427)	(346)
Unwinding of discount on liabilities	(25)	(16)
Fair value adjustments	1	–
	(451)	(362)

Finance income increased compared with 2004 predominantly due to higher interest rates and higher cash balances. Finance costs increased due to higher interest rates as well as higher interest costs resulting from the issue of two €750 million bonds in 2005.

Taxation

	2005 £m	2004 £m
UK corporation tax	172	148
Overseas taxation	1,847	1,519
Current taxation	2,019	1,667
Deferred taxation	(103)	90
Total	1,916	1,757

The charge for taxation on profit, amounting to £1,916 million, represents an effective tax rate of 28.5% (2004 – 30.4%). The tax rate in 2005 of 28.5% benefited from higher tax relief on the actual or potential exercise of share options by employees, arising from the increase in the share price in the year.

The integrated nature of the Group's worldwide operations, involving significant investment in research and strategic manufacture at a limited number of locations, with consequential cross-border supply routes into numerous end-markets, gives rise to complexity and delay in negotiations with revenue authorities as to the profits on which individual Group companies are liable to tax. Disagreements with, and between, revenue authorities as to intra-Group transactions, in particular the price at which goods should be transferred between Group companies in different tax jurisdictions, can produce conflicting claims from revenue authorities as to the profits to be taxed in individual territories. Resolution of such issues is a continuing fact of life for GSK. The Group had significant open issues with the revenue authorities in the USA, UK, Japan and Canada, details of which are set out in Note 12 to the financial statements, 'Taxation'.

Profit for the year

	2005 £m	2004 £m	Growth	
			CER%	£%
Profit after taxation for the year	4,816	4,022	17	20
Profit attributable to shareholders	4,689	3,908	17	20
Earnings per share (pence)	82.6p	68.1p	18	21
Earnings per ADS (US\$)	\$3.00	\$2.49	18	21
Weighted average number of shares (millions)	5,674	5,736		
Diluted earnings per share (pence)	82.0p	68.0p		
Diluted earnings per ADS (US\$)	\$2.98	\$2.49		
Weighted average number of shares (millions)	5,720	5,748		

Profit for the year was £4,816 million, an increase of 17% (20% in sterling terms). Profit attributable to minority interests was £127 million and profit attributable to shareholders was £4,689 million, an increase of 17% (20% in sterling terms).

Earnings per share increased 18%, reflecting higher profits and also the reduction in the weighted average number of shares resulting from the Group's share buy-back programme. The interest cost of this programme also impacts the Group's earnings.

At actual rates of exchange, earnings per share increased 21%. The favourable currency impact on EPS of three percentage points reflects a strengthening of the US dollar and Euro average exchange rates relative to 2004 and compares with a 1% favourable currency impact on turnover. This difference principally arises from a different mix of currencies in profits compared with turnover.

Corporate governance

This section discusses GlaxoSmithKline's management structures and governance procedures.

It contains the company's reporting disclosures on corporate governance required by the Combined Code on Corporate Governance of the Financial Reporting Council (Combined Code), including the required statement of compliance.

Further, the company reports on compliance with the US laws and regulations that apply to it.

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The Board

Sir Christopher Gent (Aged 58)

Appointed on 1st June 2004. Chairman. Sir Christopher was the Chief Executive Officer of Vodafone Group plc, until his retirement in July 2003. He is a Non-Executive Director of Lehman Brothers Holdings Inc, a Non-Executive Director of Ferrari S.p.A., a member of KPMG's Chairman's Advisory Group, a member of the Financial Reporting Council, a Senior Adviser at Bain & Co. and a member of the advisory board of Reform.

Dr Jean-Pierre Garnier (Aged 59)

Appointed on 23rd May 2000. Chief Executive Officer. Dr Garnier was appointed an Executive Director of SmithKline Beecham plc in 1992, and became Chief Executive Officer in April 2000. He is a Non-Executive Director of United Technologies Corporation and a member of the Board of Trustees of the Eisenhower Exchange Fellowships. He holds a PhD in pharmacology from the University of Louis Pasteur in France and an MBA from Stanford University in the USA.

Dr Stephanie Burns (Aged 52)

Appointed on 12th February 2007. Non-Executive Director. Dr Burns is Chairman, President and Chief Executive Officer of Dow Corning Corporation. She is also a member of the American Chemical Society and sits on the Executive Committee of the Society of Chemical Industry, America Section, serves on the American Chemistry Council, on the Board of Directors for the Society for Women's Health Research and on the Board of Trustees of The Conference Board. Dr Burns holds a PhD in organic chemistry from Iowa State University.

Lawrence Culp (Aged 43)

Appointed on 1st July 2003. Non-Executive Director. Mr Culp is President and Chief Executive Officer of Danaher Corporation. Prior to joining Danaher, he held positions in Accenture, previously Andersen Consulting.

Sir Crispin Davis (Aged 57)

Appointed on 1st July 2003. Non-Executive Director. Sir Crispin is Chief Executive of Reed Elsevier PLC. Prior to that, he was Chief Executive of Aegis Group plc, which he joined from Guinness plc, where he was a member of the main board and Group Managing Director of United Distillers. He spent his early career with Procter & Gamble.

Julian Heslop (Aged 53)

Appointed on 1st April 2005. Chief Financial Officer. Mr Heslop joined Glaxo Wellcome as Financial Controller in April 1998. In January 2001, following the merger, he was appointed Senior Vice President, Operations Controller. Prior to joining Glaxo Wellcome, he held senior finance roles at Grand Metropolitan PLC.

Sir Deryck Maughan (Aged 59)

Appointed on 1st June 2004. Non-Executive Director. Sir Deryck is a Managing Director of Kohlberg Kravis Roberts & Co. He was formerly Chairman and CEO of Citigroup International and of Salomon Brothers Inc. He is a Non-Executive Director of Reuters Group plc and BlackRock Inc. as well as serving on the Boards of Directors of Carnegie Hall, Lincoln Center and NYU Medical Center. He served as Vice Chairman of the New York Stock Exchange from 1996 to 2000.

Dr Daniel Podolsky (Aged 53)

Appointed on 1st July 2006. Non-Executive Director. Dr Podolsky is Mallinkrodt Professor of Medicine and Chief of Gastroenterology at Massachusetts General Hospital and Harvard Medical School as well as Chief Academic Officer of Partners HealthCare System. He is past editor-in-chief of the journal Gastroenterology, Past President of the American Gastroenterological Association and Chairman of the Board and Scientific Co-Founder of the GI Company.

Sir Ian Prosser (Aged 63)

Appointed on 23rd May 2000. Senior Independent Director. Sir Ian was formerly a Non-Executive Director of SmithKline Beecham plc. He was Chairman and Chief Executive of Bass plc and ultimately Chairman of the demerged InterContinental Hotels Group plc. He was Chairman of the World Travel and Tourism Council and the London Stock Exchange Listed Advisory Council. He is Non-Executive Deputy Chairman of BP plc, a Non-Executive Director of Sara Lee Corporation and a member of the CBI President's Committee.

Dr Ronaldo Schmitz (Aged 68)

Appointed on 23rd May 2000. Non-Executive Director. Dr Schmitz was formerly a Non-Executive Director of Glaxo Wellcome plc. He is a Non-Executive Director of Legal & General Group plc, a member of the Board of Directors of Rohm and Haas Company and Cabot Corporation and a member of the Supervisory Board of SICK AG.

Dr Moncef Slaoui (Aged 47)

Appointed on 17th May 2006. Chairman, Research & Development. Dr Slaoui joined GSK Biologicals in 1988 where he engineered the development of a robust vaccines pipeline. He has a PhD in Molecular Biology and Immunology from Université Libre de Bruxelles.

Tom de Swaan (Aged 60)

Appointed on 1st January 2006. Non-Executive Director. Mr de Swaan was a member of the Managing Board and Chief Financial Officer of ABN AMRO until 1st January 2006. He was a Non-Executive Director of the Financial Services Authority. He is a member of the Board of Directors of Zurich Financial Services in Switzerland and a member of the Supervisory Board of Royal DSM and Buhmann in the Netherlands. He is Chairman of the Board of the Netherlands Opera and a member of the Board of the Royal Concertgebouw Orchestra.

Sir Robert Wilson (Aged 63)

Appointed on 1st November 2003. Non-Executive Director. Sir Robert is Non-Executive Chairman of BG Group plc and The Economist Group and was previously Executive Chairman of Rio Tinto.

Other Directors

Dr Lucy Shapiro, formerly Non-Executive Director, retired from the Board on 17th May 2006. Dr Tachi Yamada, formerly Chairman, Research & Development, retired from the Board on 31st May 2006.

Details of membership of the Board Committees may be found on page 57.

Corporate Executive Team (CET)

JP Garnier

Chief Executive Officer

As Chief Executive Officer, Dr Garnier is responsible for the management of the Group. He oversees all operational aspects of the Group, including establishing policies, objectives and initiatives, and he directs long-term strategy. He was formerly Chief Executive Officer of SmithKline Beecham, having joined the Group in 1990.

Rupert Bondy

Senior Vice President and General Counsel

Mr Bondy is responsible for legal matters across the Group, together with environmental, health and safety issues and security. He was a lawyer in private practice before joining SmithKline Beecham in 1995.

John Clarke

President, Consumer Healthcare

Mr Clarke is responsible for the Consumer Healthcare business which produces oral, over-the-counter and nutritional healthcare products. He joined Beecham in 1976 and was the President of the Futures Group before his current appointment in January 2006.

Marc Dunoyer

President, Pharmaceuticals Japan

Mr Dunoyer was appointed President, Pharmaceuticals Japan in March 2003. He joined the Group in 1999 and was Senior Vice President and Regional Director, Japan until his current appointment.

Russell Greig

President, Pharmaceuticals International

Dr Greig leads the pharmaceutical operations outside the USA, Japan and most of Europe, covering more than 100 countries. He joined the Group in 1980 and was Senior Vice President, Worldwide Business Development for R&D prior to his current appointment in March 2003.

Julian Heslop

Chief Financial Officer

Mr Heslop became Chief Financial Officer on 1st April 2005. As head of the finance function Mr Heslop is responsible for activities such as financial reporting and control, tax and treasury, finance systems, internal audit, insurance and real estate. He joined Glaxo Wellcome as Financial Controller in April 1998.

Duncan Learmouth

Senior Vice President, Corporate Communications and Community Partnerships

Mr Learmouth is responsible for the Group's investor relations, internal and external communications, its image and partnerships with global communities. He joined Glaxo in 1991 and was Vice President, Global Investor Relations, before appointment to his current position in July 2006.

Bill Louv

Chief Information Officer

Mr Louv succeeded Dr Calhoun as Chief Information Officer on 31st January 2007. He is responsible for information technology, a global function that enables key business processes across all parts of the Group. He joined the company in 1994 and has held a number of increasingly senior roles in IT, including for US Pharmaceuticals and GSK's R&D functions.

Dan Phelan

Senior Vice President, Human Resources

Mr Phelan is responsible for benefits, compensation, recruitment, organisation development, leadership development and succession planning, human resource information systems and employee health management. He was a lawyer in private practice before joining Smith Kline & French in 1981.

David Pulman

President, Global Manufacturing and Supply

Dr Pulman is responsible for the Global Manufacturing and Supply Organisation and Global Procurement. He joined Glaxo in 1978 and was responsible for the North American supply network, manufacturing strategy and logistics until his current appointment in 2002.

Moncef Slaoui

Chairman, Research & Development

Dr Slaoui leads the Group's complex drug discovery and development activities. He joined the Group in 1988 and was Senior Vice President, Worldwide Business Development until his current appointment in June 2006.

David Stout

President, Pharmaceutical Operations

Mr Stout is responsible for all pharmaceuticals and vaccines operations worldwide, including the USA, Europe, International, Japan and Global Manufacturing and Supply. He joined SmithKline Beecham in 1996 and was President, US Pharmaceuticals, until his current appointment in January 2003.

Chris Viehbacher

President, US Pharmaceuticals

Mr Viehbacher is responsible for US Pharmaceuticals. He joined Wellcome in 1988 and was responsible for GSK's European Pharmaceuticals business before his current appointment in 2003.

Andrew Witty

President, Pharmaceuticals Europe

Mr Witty is responsible for the Group's pharmaceuticals operations in Europe. He joined Glaxo in 1985 and was Senior Vice President, Asia Pacific until his current appointment in 2003.

Other members

Mr Ziegler retired as head of the Consumer Healthcare business on 31st January 2006. Mrs Younger left the Group in June 2006 and Dr Calhoun retired as Chief Information Officer on 31st January 2007. Mr Ingram continues to act as a special consultant to the Group and attends CET meetings in that capacity.

Governance and policy

The Board and Corporate Executive Team

The Directors are listed under 'The Board' on page 54.

The Board is responsible for the Group's system of corporate governance and is ultimately accountable for the Group's activities, strategy and financial performance.

The Chief Executive Officer (CEO) is responsible for executive management of the Group and is assisted by the CET. The CET meets 11 times per year and otherwise as necessary. The members and their responsibilities are listed under 'Corporate Executive Team' (page 55).

The Board comprises three Executive and ten Non-Executive Directors. The Board considers all its Non-Executive Directors to be independent in character and judgement. Dr Schmitz has served on the Board for more than nine years, having been appointed to the Board of Glaxo Wellcome plc on 1st January 1997. During consideration of the Annual Review of Board effectiveness at its meeting in December 2006, the Board concluded that Dr Schmitz remained independent, notwithstanding his length of service. In the opinion of the Board, Dr Schmitz continued to demonstrate the characteristics of independence, such as objectively challenging management and taking part in rigorous debate, while at the same time possessing an outstanding knowledge of the company's business and affairs, together with his experience gained as Chairman of the Audit Committee. In a long cycle investment business, such as GSK, it was considered to be particularly important to have experienced members on the Board. When Sir Christopher Gent was appointed to the Board as Deputy Chairman, he was determined by the Board to be independent. Upon taking up the chairmanship of the Board on 1st January 2005, in accordance with the Combined Code, he was excluded from the determination of whether at least half the Board are independent Non-Executive Directors. Sir Christopher Gent did not hold a position on a Board Committee where independence was required under the Combined Code. He has however been appointed a member of the Remuneration Committee effective 1st January 2007 following the recent change to the Combined Code.

The Board considers that Dr Burns, Mr Culp, Sir Crispin Davis, Sir Deryck Maughan, Dr Podolsky, Sir Ian Prosser, Dr Schmitz, Mr de Swaan and Sir Robert Wilson are independent in accordance with the recommendations of the Combined Code.

At the date of publication and throughout 2006, a majority of the Board members, excluding the Chairman, were independent Non-Executive Directors. Dr Shapiro, who left the Board on 17th May 2006 was not considered to be independent due to the remuneration that she received from the Group as a member of the GlaxoSmithKline Scientific Advisory Board.

Sir Christopher Gent succeeded Sir Christopher Hogg on 1st January 2005 and chaired the company throughout 2006. Dr Garnier is the CEO. The Chairman leads the Board, and represents the Board to the CEO and other CET members as necessary between Board meetings. The CEO manages the Group and implements the strategy and policies adopted by the Board. The Chairman and the chairmen of Board Committees communicate regularly with the CEO and other CET members. The division of responsibilities between the role of Chairman and the CEO has been set out in writing, agreed by the Board and appears in full on the company's website.

Sir Ian Prosser was appointed Senior Independent Director (SID) on 1st January 2005 and held this role throughout 2006.

Board process

The Board has the authority, and is accountable to shareholders, for ensuring that the company is appropriately managed and achieves the strategic objectives it sets. The Board discharges those responsibilities through an annual programme of meetings which includes the approval of overall budgetary planning and business strategy. The Board reviews the company's internal controls and risk management policies and approves its governance structure and code of ethics.

The Board appraises and approves major financing, investment and licensing decisions in excess of defined thresholds. In addition, the Board evaluates and monitors the performance of the Group as a whole. This includes:

- engaging at Board meetings with the CEO, the other Executive Directors and members of the CET as appropriate, on the financial and operating performance of GSK and external issues material to the Group's prospects
- evaluating progress toward the achievement of the Group's financial and business objectives and annual plans
- monitoring, through reports received directly or from various committees, the significant risks facing the Group.

The Board has overall responsibility for succession planning for the CEO and the other Executive Directors. The Board has given the CEO broad authority to operate the business of the Group, and the CEO is accountable for, and reports to the Board on, business performance.

CET members make regular presentations to the Board on their areas of responsibility, and the Board meets with all the CET members on an annual basis to discuss collectively the Group's strategy.

A primary element of the induction process for new Non-Executive Directors is undertaken by members of the CET, and all Non-Executive Directors are encouraged to have separate informal discussions at their discretion with any CET members.

The Board met six times in 2006, with each member attending as follows:

Name	Number of meetings held whilst a Board member	Number of meetings attended
Sir Christopher Gent	6	6
Dr JP Garnier	6	6
Mr J Heslop	6	6
Dr M Slaoui	4	4
Mr L Culp	6	5
Sir Crispin Davis	6	6
Sir Deryck Maughan	6	4
Dr D Podolsky	3	3
Sir Ian Prosser	6	5
Dr R Schmitz	6	6
Mr T de Swaan	6	5
Sir Robert Wilson	6	6
Dr T Yamada	3	3
Dr L Shapiro	3	3

In addition to the six scheduled meetings, the Board also met on a quorate basis on three occasions.

Business environment development

To ensure that the Board is kept up-to-date on important matters, including legal, governance and regulatory developments, presentations are made on a regular basis by both external and internal advisers.

Independent advice

The Board recognises that there may be occasions when one or more of the Directors feel it is necessary to take independent legal and/or financial advice at the company's expense. There is an agreed procedure to enable them to do so. This is explained in the Corporate Governance section of the company's website.

Indemnification of Directors

Qualifying third party indemnity provisions (as defined in section 309B(1) of the Companies Act 1985) are in force for the benefit of the Directors and former Directors who held office during 2006.

Company Secretary

The Company Secretary is responsible to the Board and is available to individual Directors in respect of Board procedures. The Company Secretary is Simon Bicknell, who was appointed in May 2000. He is a barrister and joined the Group in 1984. He is secretary to all the Board Committees.

Board Committees

The Board has established a number of Committees and provides sufficient resources to enable them to undertake their duties. Executive Directors are not members of the Audit, Remuneration, Nominations or Corporate Responsibility Committees, although they may be invited to attend meetings. Each Director is a member of the Corporate Administration & Transactions and Financial Results Committees. Membership of these Committees is shown in the table below.

	Audit	Remuneration	Nominations	Corporate Responsibility
Sir Christopher Gent	–	M	C	C
Dr Burns	–	–	–	–
Mr L Culp	–	M	–	–
Sir Crispin Davis	–	M	–	–
Sir Deryck Maughan	M	–	–	–
Dr D Podolsky	M	–	–	M
Sir Ian Prosser	M	–	M	M
Dr R Schmitz*	M	M	M	–
Mr T de Swaan*	C	–	–	M
Sir Robert Wilson	M	C	–	–

* Mr de Swaan succeeded Dr Schmitz as Chairman of the Audit Committee from September 2006.

Key: C = Chairman. M = Member.

The following is a summary of the role and terms of reference of each Committee. The current full terms of reference of each Committee may be obtained from the Company Secretary or the Governance section of the company's website.

Audit Committee

The Audit Committee reviews the financial and internal reporting process, the system of internal controls, the management of risks and the external and internal audit process. The Committee also proposes to shareholders the appointment of the external auditors and is directly responsible for their remuneration and oversight of their work. The Committee consists entirely of independent Non-Executive Directors. It meets at least four times a year and otherwise as necessary. The Audit Committee Report is on pages 60 to 62.

Remuneration Committee

The Remuneration Committee determines the terms of service and remuneration of the Executive Directors and members of the CET and, with the assistance of external independent advisors, it evaluates and makes recommendations to the Board on overall executive remuneration policy. The Committee consists entirely of independent Non-Executive Directors, together with the Chairman, in accordance with the Combined Code. It meets at least four times a year and otherwise as necessary. Information on the remuneration of Directors is given in the Remuneration Report on pages 65 to 82.

The Chairman of the company and the CEO are responsible for evaluating and making recommendations to the Board on the remuneration of the Non-Executive Directors.

Nominations Committee

The Nominations Committee reviews the structure, size and composition of the Board and the appointment of members to the Board and the CET, and makes recommendations to the Board as appropriate. The Committee also monitors the planning of succession to the Board and Senior Management. The Committee consists entirely of Non-Executive Directors, of whom a majority are independent, and meets at least once a year and otherwise as necessary. The Nominations Committee Report is given on page 62.

Corporate Responsibility Committee

The Corporate Responsibility Committee consists entirely of Non-Executive Directors and provides a Board-level forum for the regular review of external issues that have the potential for serious impact upon the Group's business and reputation and for the oversight of reputation and the views of external stakeholders. The Committee is also responsible for governance oversight of the Group's worldwide donations and community support. The Committee meets formally three times a year and otherwise as necessary.

Financial Results Committee

The Financial Results Committee reviews and approves, on behalf of the Board, the Annual Report and Form 20-F, the Annual Review and the convening of the Annual General Meeting, together with the preliminary and quarterly statements of trading results. Each Director is a member of the Committee and the quorum for a meeting is any three members. To be quorate, each meeting must include the Chairman or the Chairman of the Audit Committee and the CEO or the Chief Financial Officer (CFO). The Committee meets as necessary.

Corporate governance

continued

Corporate Administration & Transactions Committee

The Corporate Administration & Transactions Committee reviews and approves matters in connection with the administration of the Group's business, and certain corporate transactions. The Committee consists of the Directors, CET members and the Company Secretary. The Committee meets as necessary.

Evaluation of the Board, Board Committees and Directors

The performance evaluation of the Board, its Committees and Directors during 2006 was undertaken by the SID and implemented in collaboration with the Committee Chairmen, with the support of the Company Secretary. The Board considered the review conclusions at its meeting in December 2006 and agreed a number of minor improvements to its procedures and operating methodology.

An external consultant was appointed to assist in the evaluation of the Audit Committee.

Dialogue with shareholders

Financial results are announced quarterly.

The company reports formally to shareholders twice a year, when its half-year and full-year results are announced. The full-year results are included in the company's Annual Report and Annual Review, which are published for shareholders. The company's half-year results are published in a national newspaper shortly after release. The CEO, CFO and President, Pharmaceutical Operations give presentations on the full-year results to institutional investors, analysts and the media.

There are webcast teleconferences after the release of the first, second and third quarter results for institutional investors, analysts and the media. The Annual Report, Annual Review and quarterly results are available on the company's website.

The Annual General Meeting (AGM) takes place in London, and formal notification is sent to shareholders at least one month in advance. At the Meeting, a business presentation is made to shareholders and all Directors able to attend are available, formally during the AGM, and informally afterwards, for questions. Committee Chairmen ordinarily attend the AGM to respond to shareholders' questions. The entire Board was in attendance at the company's AGM in May 2006. All resolutions at the AGM are decided on a poll as required by the company's Articles of Association. The results of the poll are announced to the London Stock Exchange and posted on the company's website. Details of the 2007 AGM are set out in the section 'Annual General Meeting' (see page 59).

To ensure that the Non-Executive Directors are aware of and understand the views of major shareholders about the company, the Board has in place a process focusing on sector-specific issues, as well as general shareholder preferences. At its meeting in September, the Board received an external review of shareholder opinion.

The CEO and CFO maintain a dialogue with institutional shareholders on performance, plans and objectives through a programme of regular meetings.

The Group's Investor Relations department, with offices in London and Philadelphia, acts as a focal point for contact with investors throughout the year.

The Chairman meets regularly with institutional investors to hear their views and discuss issues of mutual importance.

The Chairman of the Remuneration Committee meets annually with major shareholders to discuss executive remuneration policy.

All Non-Executive Directors, including new appointees, are available to meet with major shareholders if requested.

The company's website provides access to current financial and business information about the Group.

Share buy-back programme

The company has repurchased £7.8 billion of its own shares for cancellation or to be held as Treasury shares, of which £1.3 billion was spent in 2006. In October 2006, a programme totalling £6 billion of share repurchases over three years commenced. It is expected that £2 billion worth of shares will be brought back in the first 12 months. These programmes cover purchases by the company of shares for cancellation or to be held as Treasury shares, in accordance with the authority renewed by shareholders at the company's AGM in 2006.

In May 2006, the company was authorised to purchase a maximum of 582 million shares. During 2006, 92.6 million shares, representing 1.7% of the issued share capital, were purchased and held as Treasury shares (see Note 31 to the financial statements, 'Share capital and share premium account').

The exact amount and timing of future purchases, and the extent to which repurchased shares will be held as Treasury shares rather than being cancelled, will be determined by the company and is dependent on market conditions and other factors.

Donations to Political Organisations and EU Political Expenditure

At the AGM in May 2001, shareholders first authorised the company to make donations to EU Political Organisations and to incur EU Political Expenditure, under the provisions of the Political Parties, Elections and Referendums Act 2000, of up to £100,000 each year. This authority has since been renewed annually. Although the company does not make and does not intend to make such payments or donations to EU political parties, within the normal meaning of that expression, the definition in the legislation of 'EU Political Organisation' is wide. It may extend to bodies, which the company and its subsidiaries might wish to support including those concerned with policy review, law reform, the representation of the business community and special interest groups, such as those concerned with the environment. No donations were made to EU Political Organisations during 2006. The Group made donations to non-EU Political Organisations totalling £319,000 during 2006 (£320,000 in 2005).

Donations of £290,000 (£301,000 in 2005) were made in the USA, £27,000 (£19,000 in 2005) in Canada and £2,000 in Australia. The USA is the largest recipient of political donations, and this reflects the US political system, where candidates are sponsored solely by donations from individuals, NGOs, companies and other parties.

In line with US law, the corporate donations by GSK are not made at a federal level, but only to candidates and political parties at the state and local levels. Donations are accepted practice in the USA, and as a major employer in a heavily regulated industry, it is important for GSK to engage fully in the political process. Donations are one of the ways of doing this. GSK supports those candidates who seek an environment that appropriately rewards high-risk, high-investment industries and who believe in free market principles and intellectual property rights.

The situation is similar in Canada, and donations follow the same guidelines. In the rest of the world donations are very rare and of low value.

There is also a GSK Political Action Committee (PAC) in the USA which gives political donations. PAC's are employee organisations which allow employees to contribute to a fund for political donations. Employees decide upon the recipients of the PAC donations. In 2006, a total of £735,600 (£282,000 in 2005) was donated to political organisations by the GSK PAC.

Annual General Meeting

The AGM will be held at 2.30pm on Wednesday, 23rd May 2007 at The Queen Elizabeth II Conference Centre, Broad Sanctuary, Westminster, London SW1P 3EE. The business to be transacted at the meeting will include:

- **Receiving and adopting GlaxoSmithKline's 2006 Annual Report**
- **Approving the 2006 Remuneration Report**
The Remuneration Report on pages 65 to 82 sets out the remuneration policies operated by GlaxoSmithKline and disclosures on Directors' remuneration, including those required by the Companies Act 1985 and the Directors' Remuneration Report Regulations 2002. A resolution will be proposed to approve the Remuneration Report.
- **Retirement, election and re-election of Directors**
Dr Podolsky and Dr Burns have been appointed Directors since the 2006 AGM and will offer themselves for election to the Board. Mr Heslop, Sir Deryck Maughan, Dr Schmitz and Sir Robert Wilson will each retire and offer themselves for re-election to the Board under article 93 of the company's Articles of Association.
- **Re-appointment and remuneration of Auditors**
Resolutions will be proposed to re-appoint PricewaterhouseCoopers LLP as auditors and to authorise the Audit Committee to determine their remuneration.

- **Special business**

The company will seek authority to:

- make donations to EU Political Organisations and incur EU Political Expenditure
- allot Ordinary Shares in the company
- give the Directors authority to disapply pre-emption rights when allotting new Shares in connection with rights issues or otherwise up to a maximum of 5% of the current issued share capital and purchase its own Ordinary Shares up to a maximum of just under 10% of the current issued share capital
- amend the company's Articles of Association to enable electronic communication with shareholders, in accordance with the new Companies Act 2006.

Internal control framework

The Board recognises its responsibility to present a balanced and understandable assessment of the Group's position and prospects. The structure of accountability and audit operated in GSK is as follows.

The Board has accountability for reviewing and approving the adequacy and effectiveness of internal controls operated by the Group, including financial, operational and compliance controls and risk management. The Board has delegated responsibility for such review to the Audit Committee, which receives reports from those individuals identified in the Committee's Report on pages 60 to 62. It is the responsibility of management, through the CET, to implement Board policies on risk and control. The CET is responsible for identifying, approving, monitoring and enforcing key policies that go to the heart of how the Group conducts business. The internal control framework includes central direction, resource allocation and risk management of the key activities of research and development, manufacturing, marketing and sales, legal, human resources, information systems and financial practice. As part of this framework, there is a comprehensive planning system with an annual budget approved by the Board. The results of operating units are reported monthly and compared to the budget. Forecasts are prepared regularly during the year.

Extensive financial controls, procedures, self-assessment exercises and risk activities are reviewed by the Group's internal auditors. Commercial and financial responsibility, however, is clearly delegated to local business units, supported by a regional management structure. These principles are designed to provide an environment of central leadership coupled with local operating autonomy as the framework for the exercise of accountability and control within the Group.

The Group also attaches importance to clear principles and procedures designed to achieve appropriate accountability and control. A Group policy, 'Risk Management and Legal Compliance', mandates that business units establish processes for managing and monitoring risks significant to their businesses and the Group.

The internal control framework also relies on the following for overseeing and reporting risk and compliance issues.

Corporate governance

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Risk Oversight and Compliance Council (ROCC)

The ROCC is a council of senior executives authorised by the Board to assist the Audit Committee oversee the risk management and internal control activities of the Group. Membership comprises several CET members and some of the heads of departments with internal control, risk management, audit and compliance responsibilities.

The ROCC meets on a regular basis to review and assess significant risks and their mitigation plans. The ROCC, responding to the Group policy referred to above, has provided the business units with a framework for risk management and upward reporting of significant risks. Mitigation planning and identification of a manager with overall responsibility for management of any given risk is a requirement.

Risk Management and Compliance Boards (RMCBs)

Risk Management and Compliance Boards (RMCBs) have been established in each of the major business units. Membership often comprises members of the senior executive team of the respective business unit, augmented by specialists where appropriate. The RMCBs oversee management of all risks that are considered important for their respective business units, including those risks that are designated as significant to GlaxoSmithKline as a whole, thus increasing the number of risks that are actively managed across the Group.

Each RMCB regularly reports the status regarding its significant risks to the ROCC.

Compliance functions

In a number of risk areas, specific standards that meet or exceed requirements of applicable law have been established. Specialist audit and compliance functions (for example: Corporate Environment, Health & Safety, Global Quality Assurance and Worldwide Regulatory Compliance) assist in the dissemination, implementation and audit of these standards.

Corporate Ethics & Compliance (CEC)

The ROCC is also supported by the Corporate Ethics & Compliance department which is responsible for supporting the development and implementation of practices that facilitate employees' compliance with laws and Group policy.

The thrust of the Group's compliance effort is due diligence in preventing and detecting misconduct and non-compliance with law or regulation by promoting ethical behaviour, compliance with all laws and regulations, corporate responsibility at all levels and effective compliance systems.

The CEC is managed by the Corporate Compliance Officer, who reports directly to the CEO. The Corporate Compliance Officer chairs the ROCC and provides summary reports on the ROCC's activities and the Group's significant risks to the CET and the Audit Committee on a regular basis. The Corporate Compliance Officer's direct reporting line to the Audit Committee provides a mechanism for bypassing the executive management should the need ever arise.

Areas of potentially significant risk

For details of risks affecting the Group, see 'Risk factors' on pages 44 to 47 and Note 43 to the financial statements, 'Legal proceedings'.

Effectiveness of controls

The internal control framework has been in operation for the whole of the year under review and continues to operate up to the date of approval of this report. The system of internal controls is designed to manage rather than eliminate the risk of not achieving business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss.

The Audit Committee receives reports on areas of significant risk to the Group and on related internal controls. Following consideration of these reports, the Audit Committee reports annually to the Board on the effectiveness of controls. Such controls may mitigate but cannot eliminate risks. In addition, there are areas of the Group's business where it is necessary to take risks to achieve a satisfactory return for shareholders, such as investment in R&D and in acquiring new products or businesses. In these cases, it is the Group's objective to apply its expertise in the prudent management rather than elimination of risk. The Directors' review relates to the company and its subsidiaries and does not extend to material associated undertakings, joint ventures or other investments.

The Board, through the Audit Committee, has reviewed the assessment of risks and the internal control framework that operates in GlaxoSmithKline and has considered the effectiveness of the system of internal control in operation in the Group for the year covered by this report and up to the date of its approval by the Board. The process followed by the Board in reviewing the system of internal controls accords with the guidance on internal control issued by the Turnbull Committee in 1999.

Committee reports

Audit Committee Report

The Audit Committee's role flows directly from the Board's oversight function and it is authorised by the Board to investigate any activity within its terms of reference. The Committee has written terms of reference which have been approved by the Board. The Committee reports regularly to the Board on the performance of the activities it has been assigned. The Committee's main responsibilities include reviewing the corporate accounting and financial reporting process, monitoring the integrity of the financial statements, evaluating the system of internal control and the management of risks, overseeing activities of each of the Group's compliance audit functions and overseeing compliance with laws, regulations and ethical codes of practice. The Committee's oversight role requires it to address regularly the relationships between management and the internal and external auditors, and understand and monitor the reporting relationships and tiers of accountability between them.

The Committee receives regular reports from members of the CET and senior managers covering the key compliance activities of the Group, including those concerning R&D, manufacturing, sales and marketing and EHS.

Committee members bring considerable financial and accounting experience to the Committee's work. Members have past employment experience in either finance or accounting roles or comparable experience in corporate activities.

Dr Schmitz was the Chairman of the Committee from April 2001 until September 2006. Prior to his appointment as a Non-Executive Director of the company, he was a Non-Executive Director of Glaxo Wellcome plc, where he served on the Audit Committee. Dr Schmitz has also been a member of the Executive Board of Directors of Deutsche Bank AG. He retired from that Board in 2000 having been in charge of investment banking. Dr Schmitz was formerly a member of the Executive Board of Directors of BASF from 1980 to 1990, including CFO from 1985 to 1990. He holds an MBA from Insead.

Mr de Swaan joined the Board and the Committee with effect from 1st January 2006. He succeeded Dr Schmitz as Chairman of the Committee with effect from September 2006. When appointing Mr de Swaan to the Committee, the Board determined that he had recent and relevant financial experience, in accordance with the Combined Code. In coming to this conclusion, the Board paid particular attention to Mr de Swaan's role as Chief Financial Officer of ABN AMRO, from which he retired on 31st December 2005. The Board also considers Mr de Swaan to be an Audit Committee Financial Expert as defined by Sarbanes-Oxley.

Sir Deryck Maughan is a Managing Director of Kohlberg Kravis Roberts & Co (KKR) and Chairman of KKR Asia. He was Chairman and CEO of Citigroup International and Vice Chairman of Citigroup Inc. Prior to the creation of Citigroup, he was Chairman and Co-Chief Executive Officer of Salomon Smith Barney. He was also Chairman and Chief Executive Officer of Salomon Brothers Inc..

Sir Ian Prosser was CFO and later CEO of Bass plc and is a member of the Institute of Chartered Accountants in England and Wales.

Sir Robert Wilson began his professional career as an economist. He is Chairman of BG Group plc. He held senior management positions at Rio Tinto plc culminating in his appointment as Executive Chairman, from which he retired in 2003.

Dr Daniel Podolsky was appointed to the Committee with effect from 1st January 2007. He is a world-renowned researcher who has advanced knowledge of underlying mechanisms of disease and new therapies for gastrointestinal disorders. His background will enable him to bring scientific expertise to the Committee's deliberations.

The Committee is supported by the Company Secretary, who attends the Committee's meetings, and it has available to it financial resources to take independent professional advice when considered necessary. Meetings of the Committee are attended by the Chairman, CEO, CFO, General Counsel, Head of Global Internal Audit (GIA), Corporate Compliance Officer and the external auditors.

In 2006, the Committee worked to a structured programme of activities, with standing items that the Committee is required to consider at each meeting together with other matters focused to coincide with key events of the annual financial reporting cycle:

- the external auditors reported to the Committee on all critical accounting policies and practices used by the company, alternative accounting treatments which had been discussed with management and the resultant conclusion by the external auditors, material written communications with management and any restrictions on access to information
- the CFO reported on the financial performance of the company and on technical financial and accounting matters
- the General Counsel reported on material litigation
- the Company Secretary reported on corporate governance
- the Heads of each of the Group's compliance and audit groups reported on their audit scope, annual coverage, audit resources and on the results of audits conducted throughout the year
- the Corporate Compliance Officer reported on the activities undertaken by the ROCC
- the Company Secretary, as Chairman of the Disclosure Committee, reported on matters that affected the quality and timely disclosure of financial and other material information to the Board, to the public markets and to shareholders. This enabled the Committee to review the clarity and completeness of the disclosures in the published annual financial statements, interim reports, quarterly and preliminary results announcements and other formal announcements relating to financial performance prior to their release by the Board.

The Audit Committee, management, internal auditors and the full Board work together to ensure the quality of the company's corporate accounting and financial reporting. The Committee serves as the primary link between the Board and the external and internal auditors. This facilitates the necessary independence from management and encourages the external and internal auditors to communicate freely and regularly with the Committee. In 2006, the Committee met both collectively and separately with the external auditors and the Head of GIA, without members of management being present.

The Committee has primary responsibility for making a recommendation to shareholders on the appointment, reappointment and removal of the external auditors by annually assessing the qualifications, expertise, resources and independence of the external auditors and the effectiveness of the audit process.

In making its assessment, the Committee considers papers which detail the relevant regulatory requirements relating to external auditors and evaluates reports from the external auditors on their compliance with the requirements. Where the external auditors provide non-audit services, the Committee ensures that auditor objectivity and independence are safeguarded by a policy requiring pre-approval by the Audit Committee for such services. These services may include audit services, audit-related services, tax services and other services. Pre-approval is detailed as to the particular service or categories of services, and is subject to a specific budget. The external auditors and management report regularly to the Committee regarding the extent of services provided in accordance with this pre-approval and the fees for the services performed. The Committee may also pre-approve additional services on a case-by-case basis. Expenditure on audit and non-audit services is set out in Note 7 to the financial statements 'Operating profit'.

The guidelines set out in the company's policy on engaging the external auditors to provide non-audit services include ascertaining that: the skills and experience of the external auditors make them a suitable supplier of the non-audit services; adequate safeguards are in place so that the objectivity and independence of the audit are not compromised; and the fee levels relative to the annual audit fee are within the limits set by the Committee.

The company also has well-established policies, including a Code of Ethics, which is available on its website, and a help-line facility for the reporting and investigation of unlawful conduct. No waivers to the Code were made in 2006.

The Committee met in full session five times in 2006 and five times on a quorate basis. Each full session was attended by all members except Mr de Swaan and Sir Deryck Maughan who were each unable to attend one meeting.

Nominations Committee Report

The Nominations Committee's terms of reference include responsibility for proposing the appointment of Board and Committee members. During 2006, the Committee made recommendations to the Board on the appointment of Dr Podolsky as a Non-Executive Director and Scientific/Medical expert.

In February 2006, the Committee recommended to the Board that Dr Moncef Slaoui, would succeed Dr Yamada as Chairman, Research & Development, on his retirement from the company on 31st May 2006.

In February 2007, the Committee with the Board's approval, appointed Dr Stephanie Burns as a Non-Executive Director.

When recruiting Non-Executive Directors, the Committee considers the particular skills, knowledge and experience that would benefit the Board most significantly for each appointment. Broad selection criteria are used which focus on achieving a balance between the representation of European, UK and US markets, and having individuals with CEO experience and skills developed in various sectors and specialities. During 2006, particular focus was placed upon recruiting a Non-Executive with scientific and medical expertise. Professional search agencies are engaged specialising in the recruitment of high calibre Non-Executive Directors. Dossiers of potential Non-Executive appointees are provided to the Committee and candidates are short-listed for interview after considering their relevant qualifications.

A customised induction process is conducted for each of the new Non-Executive Directors focusing on their particular experience and taking account of their different backgrounds. This process includes meeting members of the CET and other senior executives and visiting particular operational facilities of the Group.

The Committee continued to keep under review the succession planning for senior executive positions, including that of the CEO. During 2006, the Committee agreed the process for selecting Dr Garnier's successor as CEO of GSK.

When appointing new Executive Directors, and CET members, the Committee considers the skills, knowledge and experience required for the particular executive position. The Committee will consider potential external and internal candidates before recommending to the Board to approve the new appointment. All new Directors offer themselves for election at the company's next AGM. Their appointments are announced publicly.

The Committee recommended the appointment of Dr Podolsky to the Corporate Responsibility Committee with effect from June 2006 and then to the Audit Committee with effect from 1st January 2007. The Committee also recommended the appointment of Sir Christopher Gent to the Remuneration Committee with effect from 1st January 2007.

The Committee met four times during 2006 in full session. All members were present at the full meetings.

Remuneration Report

The Remuneration Report can be found on pages 65 to 82.

Corporate Responsibility Committee Report

During the year the Corporate Responsibility Committee reviewed GSK's activity in a number of responsibility areas including access to medicines, community partnerships, reputation management, caring for the environment, ethical conduct, Direct To Consumer (DTC) advertising and GSK's commercial practices codes.

Membership of the Committee changed during the year. Following Dr Shapiro's retirement from the Board in May 2006, Tom de Swaan and Dr Daniel Podolsky joined the Committee.

The Committee met five times during 2006. Each meeting was attended by all Committee members except Sir Ian Prosser who was unable to attend one meeting, and Dr Shapiro who was unable to attend two meetings.

GSK's Corporate Responsibility Report can be accessed on www.gsk.com.

The Combined Code

Throughout 2006, the company complied with the Code provisions of the Combined Code, except as follows:

- B.1.1 – In designing schemes of performance-related remuneration, the Remuneration Committee should follow the provisions in Schedule A to the Code. Item 6 of Schedule A states that, in general, only basic salary should be pensionable. The company's position is explained in the Remuneration Report on pages 65 to 82.

US law and regulation

A number of provisions of US law and regulation apply to GSK because the company's shares are quoted on the New York Stock Exchange (NYSE) in the form of ADSs.

NYSE rules

In general, the NYSE rules permit the company to follow UK corporate governance practices instead of those applied in the USA, provided that the company explains any significant variations. This explanation is on the company's website. NYSE rules that came into effect in 2005 require the company to file annual and interim written affirmations concerning the Audit Committee and the company's statement on significant differences in corporate governance.

Sarbanes-Oxley Act of 2002

Following a number of corporate and accounting scandals in the USA, Congress passed the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley). Sarbanes-Oxley is a wide ranging piece of legislation concerned largely with financial reporting and corporate governance.

As recommended by the Securities and Exchange Commission (SEC), GSK has established a Disclosure Committee. The Committee reports to the CEO, the CFO and to the Audit Committee. It is chaired by the Company Secretary and the members consist of senior managers from finance, legal, compliance, corporate communications and investor relations.

External legal counsel and the external auditors are invited to attend its meetings periodically. It has responsibility for considering the materiality of information and, on a timely basis, determining the disclosure of that information. It has responsibility for the timely filing of reports with the SEC and the formal review of the Annual Report and Form 20-F. In 2006, the Committee met 14 times.

Sarbanes-Oxley requires that the Annual Report contains a statement as to whether a member of the company's Audit Committee is an audit committee financial expert. For an explanation and details of the basis for the Board's judgement on this matter, refer to page 61. Additional disclosure requirements arise under Section 302 and Section 404 in respect of disclosure controls and procedures, and internal control over financial reporting.

Section 302: Corporate responsibility for financial reports

Sarbanes-Oxley also introduced a requirement for the CEO and the CFO to complete formal certifications, confirming that:

- they have each reviewed the Annual Report and Form 20-F
- based on their knowledge, it contains no material misstatements or omissions
- based on their knowledge, the financial statements and other financial information fairly present, in all material respects, the financial condition, results of operations and cash flows as of the dates, and for the periods, presented in the Annual Report and Form 20-F
- they are responsible for establishing and maintaining disclosure controls and procedures that ensure that material information is made known to them, have evaluated the effectiveness of these controls and procedures as at the year end, the results of such evaluation being contained in the Annual Report and Form 20-F
- they are responsible for establishing and maintaining internal control over financial reporting that provides reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles
- they have disclosed in the Annual Report and Form 20-F any changes in internal controls over financial reporting during the period covered by the Annual Report and Form 20-F that have materially affected, or are reasonably likely to affect materially, the company's internal control over financial reporting
- they have disclosed, based on their most recent evaluation of internal control over financial reporting, to the external auditors and the Audit Committee all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to affect adversely the company's ability to record, process, summarise and report financial information and any fraud (regardless of materiality) involving persons that have a significant role in the company's internal control over financial reporting.

The Group has carried out an evaluation under the supervision and with the participation of the Group's management, including the CEO and CFO, of the effectiveness of the design and operation of the Group's disclosure controls and procedures as at 31st December 2006. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives.

The CEO and CFO expect to complete these certifications and report their conclusions on the effectiveness of disclosure controls and procedures on 2nd March 2007, following which the certificates will be filed with the SEC as part of the Group's Form 20-F.

Corporate governance

continued

Section 404: Management's annual report on internal control over financial reporting

In accordance with the requirements of section 404 of Sarbanes-Oxley, the following report is provided by management in respect of the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the US Securities Exchange Act of 1934):

- Management is responsible for establishing and maintaining adequate internal control over financial reporting for the Group. Internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS, including the reconciliations required under US GAAP
- Management conducted an evaluation of the effectiveness of internal control over financial reporting based on the framework in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organisations of the Treadway Commission
- There have been no changes in the Group's internal control over financial reporting during 2006 that have materially affected, or are reasonably likely to affect materially, the Group's internal control over financial reporting
- Management has assessed the effectiveness of internal control over financial reporting, as at 31st December 2006, and its conclusion will be filed as part of the Group's Form 20-F
- PricewaterhouseCoopers LLP, which has audited the consolidated financial statements of the Group for the year ended 31st December 2006, has also audited management's assessment of the effectiveness of internal control over financial reporting and the effectiveness of the Group's internal control over financial reporting under Auditing Standard No. 2 of the Public Company Accounting Oversight Board (United States). Their audit report will be filed with the Group's Form 20-F.

Remuneration Report

The Remuneration Report sets out the remuneration policies operated by GSK in respect of the Directors and Corporate Executive Team (CET) members, together with disclosures on Directors' remuneration including those required by The Directors' Remuneration Report Regulations 2002 (the Regulations). In accordance with the Regulations, the following sections of the Remuneration Report are subject to audit: Annual remuneration; Non-Executive Directors' remuneration; Share options; Incentive plans; performance criteria on Performance Share Plans and share options; and Pensions for which the opinion thereon is expressed on page 166. The remaining sections are not subject to audit nor are the pages referred to from within the audited sections.

This Report is submitted to shareholders by the Board for approval at the Annual General Meeting, as referenced in the notice of Annual General Meeting.

Throughout the Remuneration Report the Executive Directors and CET members are referred to as the 'Executives'.

References to GlaxoSmithKline shares and ADSs mean, respectively, Ordinary Shares of GlaxoSmithKline plc of 25p and American Depository Shares of GlaxoSmithKline plc. Each ADS represents two GlaxoSmithKline shares.

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Remuneration Report

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Introduction

The Remuneration Committee (or Committee) is responsible for making recommendations to the Board on the company's remuneration policy and, within the terms of the agreed policy, determining the total individual remuneration packages of the Executives.

GSK's remuneration policy was agreed after an extensive consultation process with shareholders and institutional bodies during the course of 2003 and 2004. The appropriateness of the elements of the policy is kept under review by the Committee.

The Chairman of the Remuneration Committee continues to have regular dialogue with institutional investors regarding GSK's remuneration policy.

GlaxoSmithKline's remuneration policy is designed to establish a framework for remuneration that is consistent with the company's scale and scope of operations, meets the recruitment needs of the business and is closely aligned with UK shareholder guidelines. As at 31st December 2006, the company was the second largest pharmaceutical company in the world by revenue, with operations on five continents with products sold in over 140 countries and with over 50% of sales being generated in the USA.

Remuneration Committee

Sir Robert Wilson has been Chairman of the Committee since 17th May 2004. Sir Crispin Davis, Mr Culp and Dr Schmitz were members of the Committee throughout 2006. The Board deemed all of the members of the Committee to be independent Non-Executive Directors in accordance with the Combined Code.

Following the change to the Combined Code made by the Financial Reporting Council, with effect from 1st November 2006, Sir Christopher Gent was appointed a member of the Committee with effect from 1st January 2007.

The Committee met four times during 2006 with each member attending as follows:

Name	Number of meetings held whilst a Committee member	Number of meetings attended by Committee member
Sir Robert Wilson	4	4
Mr Larry Culp	4	3
Sir Crispin Davis	4	4
Dr Ronaldo Schmitz	4	4

At these meetings, amongst other items, the Committee considered:

- the terms of service and remuneration levels for new Executive appointments
- the competitiveness of the company's total reward package, including the level of annual and long-term incentive opportunity
- the effectiveness of the annual bonus plan, particularly for R&D employees
- the structure and competitiveness of US pension arrangements.

The policy aspects above were discussed by the Chairman and the Chairman of the Committee at their annual meetings with institutional investors. In addition, each year following the AGM, the Committee considers GSK's remuneration policy in the context of market and best practice.

Two quorate meetings were held during the year to approve the formal grant of share options and performance share awards in accordance with GSK remuneration policy.

With the exception of Mr Bicknell (Company Secretary), no employees of the company were involved in the conduct of Committee meetings. Dr Garnier (CEO) and Mr Phelan (Senior Vice President, Human Resources), were invited to attend part of some meetings of the Committee as required.

Deloitte & Touche LLP (Deloitte) have been appointed by the Committee to provide it with independent advice on executive remuneration.

Deloitte provided other consulting services to GSK during the year, but did not provide advice on executive remuneration matters other than to the Committee.

Towers Perrin provides market data and data analysis to the Committee.

Remuneration policy

Principles

The remuneration policy for GlaxoSmithKline is designed to secure outstanding executive talent, and to provide pay for performance and only for performance, within a transparent and robust governance structure.

The Committee determined that GSK's remuneration policy would be based on the following key principles:

- the remuneration structure must support the needs of the business in a very competitive market place
- UK shareholder guidelines will be followed to the maximum extent consistent with the needs of the business and the company would maintain a regular dialogue with shareholders
- global pharmaceutical companies are the primary pay comparator group
- performance conditions would be based on the measurable delivery of strong financial performance and the delivery of superior returns to shareholders as compared with other pharmaceutical companies
- a high proportion of the total remuneration opportunity will be based on performance-related remuneration which will be delivered over the medium to long term
- remuneration would be determined using the projected value method (see 'Benchmarking' below)
- there would be one remuneration structure for Executive Directors and the CET with the same performance conditions applying equally to their long-term incentive awards
- no ex-gratia payments will be made
- pay structures would be as simple as is consistent with the business needs.

Overall, the policy is intended to provide median total remuneration for median performance, with the opportunity to earn upper quartile total remuneration for exceptional performance. Poor performance will result in total remuneration significantly below the pay comparator group median.

This strong alignment with performance is demonstrably in the interests of shareholders and provides the Executives with unambiguous signals about the importance of delivering success to the company's shareholders.

Commitment

The Committee will apply this policy on a consistent and transparent basis. Any significant changes in the measures used to assess performance will be discussed with shareholders. In the use of comparators for pay benchmarking, the Committee will use its discretion to ensure that remuneration levels are reasonable, and if it believes that changes may cause concern amongst shareholders, the position will be discussed with shareholders prior to implementation.

Pay and performance comparators

The following table sets out the companies used for pay and performance comparison:

Company	Country	Market Cap 31.12.06 £m
Abbott Laboratories	USA	38,144
Amgen	USA	40,656
AstraZeneca	UK	42,036
Bristol-Myers Squibb	USA	26,410
Eli Lilly	USA	30,079
GlaxoSmithKline	UK	77,362
Johnson & Johnson	USA	97,661
Merck	USA	48,294
Novartis	Switzerland	77,066
Pfizer	USA	95,281
Roche Holdings	Switzerland	80,157
Sanofi-Aventis	France	64,166
Schering-Plough	USA	17,882
Takeda Pharmaceutical Company*	Japan	31,182
Wyeth	USA	34,987

* only included for performance comparison

The merger of Aventis and Sanofi-Synthelabo during 2004 reduced the size of the comparator group to 13 companies and GlaxoSmithKline. During the year, the Committee reviewed this group, as part of its continuous appraisal of GSK's remuneration arrangements and as a result determined that Amgen should be added to the group with effect from 1st January 2007.

Benchmarking

For benchmarking purposes, total remuneration incorporates base salary, annual bonus and long-term incentives. Notwithstanding this, when setting pay, the Committee also has due regard to the Executives' pension arrangements.

The global pharmaceutical industry is used as the primary pay comparator for Executives, as it is the appropriate marketplace for the company's most senior executive talent.

In the first instance, pay is benchmarked to publicly available remuneration data for these companies. To provide additional context reference is also made to the Towers Perrin annual global pharmaceutical pay survey for the Pharmaceutical Human Resources Association (PHRA). To ensure that the global pharmaceutical industry benchmark is subject to scrutiny and review, the Committee also regularly considers pay data from other global businesses primarily in the consumer and the manufacturing sectors.

Prior to determining the annual long-term incentive opportunity, the Committee considers a range of payout levels that may be achieved based on different assumptions, such as share price growth, performance levels etc.

For performance in line with expectations, total remuneration is targeted at the median of the pay comparator group and the long-term incentive opportunity is set in a way which provides for positioning of total remuneration at the median of this group.

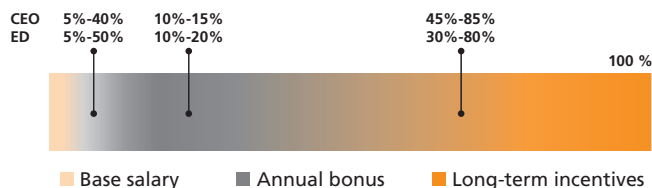
Valuation method

The projected value method is used to benchmark total remuneration. This method projects the future value of the remuneration package under different performance scenarios. This method, taken together with an assessment of the pay comparator groups' incentive policies over several years, moderates the impact of market fluctuations in the short term and strengthens the focus on performance.

Following the independent review in 2003, the Committee made a deliberate and conscious decision to use the projected value method for pay benchmarking purposes as it enables a comparison of packages with different structural characteristics and provides an insight into the value gearing of different equity instruments.

Individual elements of remuneration

The balance between the fixed (base salary) and variable (annual bonus and long-term incentive) elements of remuneration changes with performance. The chart below shows the anticipated normal range of the mix between fixed and variable pay at different levels of performance for the CEO and the typical case for the other Executive Directors (ED). In some years, the ranges may be higher or lower, depending on the performance of the company and the individual.



Base salary

Base salaries are set by reference to the median for the relevant market. For Executives, this is the pharmaceutical pay comparator group. Actual salary levels are reviewed annually and are influenced by an Executive's experience, responsibility and market value. Any changes usually take effect from 1st April.

The table below sets out base salary increases that took effect during the year and those that will take effect in April 2007.

	Base salary from 1st April 2006	Percentage increase	Base salary from 1st April 2007
Dr Garnier	\$1,730,000	6%	\$1,834,000
Mr Heslop*	£400,000	12.5%	£450,000
Dr Slaoui*	\$600,000**	21%	\$725,000

* These base salary increases reflect the Committee's assessment of performance in their respective roles since appointment.

** Dr Slaoui was appointed to the Board with effect from 17th May 2006 and succeeded Dr Yamada with effect from 1st June 2006.

Remuneration Report

continued

Annual bonus

All bonuses are determined on the basis of a formal review of annual performance against stretching financial targets based on profit before interest and tax and are subject to detailed assessment of individual, business unit and Group achievements against objectives. No bonus is payable if financial performance is less than 96% of the target. The maximum bonus that Executives can earn based solely on corporate performance is approximately two-thirds of the maximum bonus opportunity. The individual performance against objectives can increase or decrease the bonus level by a factor which can range from zero to 1.5. Bonuses are subject to upper limits which, for the Executives other than the CEO, range between 100% and 200% of base salary. The CEO's maximum bonus opportunity is 200%.

Following the review of the Annual Bonus Plan, the Committee determined that bonus measures linked to the pipeline would be introduced for R&D employees including Dr Slaoui. A robust governance structure has been established to ensure that the bonus payable under the revised arrangements fairly reflects R&D productivity and performance as well as profit targets. The Committee will review the bonus arrangements after the first year of operation.

The aim of the remuneration policy is to deliver annual cash in line with the median of the pay comparator group for on-target business performance.

In the case of the CEO, the bonus targets are set by the Board. In setting the objectives for the CEO, the Board takes into account the strategies that have been developed by the company, and are set out on page 2 of the Annual Report.

For reasons of commercial sensitivity, the specific objectives set against the strategic business drivers as set out on page 2 are kept confidential. Following the end of the financial year, the Board reviews the CEO's performance generally and against the set objectives, and the Committee then determines the bonus payable. For the other Executives, the CEO makes recommendations to the Committee regarding the performance level achieved against objectives. These recommendations are then considered by the Committee to determine the resultant bonus.

The objectives set for 2006 focused in particular on building the best product pipeline in the industry and delivering commercial and operational excellence.

The Committee took into account the company's success in achieving these objectives, as well as individual Executives' performance, when determining the bonus awards for 2006.

Long-term incentives

Executives are eligible for performance share awards and share options. The remuneration policy provides that annual long-term incentive (LTI) awards will normally be made up of a performance share award and a share option award.

The Committee considers that performance shares provide a stronger alignment to shareholder interests, and therefore the remuneration policy places greater emphasis on the use of performance shares. LTI awards are determined such that for on-target performance more than half of the LTI reward should be derived from performance shares.

The annual grant of LTI awards using more than one plan is consistent with the practice of the pay comparator group and other leading UK companies. LTIs for the CET are provided on the same basis as the Executive Directors. The level of the annual LTI opportunity is considered carefully year-on-year by the Committee in the context of market practice and GSK's policy on market positioning. Following this review in 2006, the Committee determined it appropriate to make adjustments to the LTI awards for a number of Executives in line with the policy.

To align the award cycles more closely with GSK's financial year and budgeting process, the Committee decided in 2005 to change the annual grant date for LTI awards for all eligible employees from the fourth quarter of each year to the first quarter of each year. No compensation was provided for the change in the award cycle.

Historically, the performance period for awards made in the fourth quarter started on 1st January following the date of award. For LTI awards made in 2006 and thereafter, the performance period starts on 1st January of the year of award (i.e. 1st January 2006 for awards made in February 2006).

Performance share awards and share options are delivered to US resident executives in the form of ADSs. Awards are delivered in the form of Ordinary Shares to executives resident in the UK and other countries. All awards are made under plans which incorporate dilution limits consistent with the guidelines provided by the Association of British Insurers, the National Association of Pension Funds and other shareholder representative bodies. Current estimated dilution from existing awards under all GlaxoSmithKline employee share schemes made since the merger is approximately 6.6% of the company's share capital at 31st December 2006.

a) Performance shares

For the Executives, the level of performance shares vesting is based on the company's Total Shareholder Return (TSR) relative to the performance comparator group (see page 67) over a three-year measurement period. TSR was chosen as the most appropriate comparative measure since it focuses on the return to shareholders, is a well-understood and tested mechanism to measure performance and allows comparison between companies operating in different countries.

TSR is measured in Sterling over the performance period and represents the change in the value of a share together with the value of reinvested dividends paid. In order to remove the impact of the varying tax treatments of dividends in different jurisdictions, all dividends are reinvested gross.

The table below sets out the performance share awards made in February 2007, for which full disclosure will be made in the 2007 Remuneration Report.

Executive Director	Performance share award	Market price on date of grant
Dr Garnier	240,000 ADSs	\$58.00
Mr Heslop	105,000 shares	£14.88
Dr Slaoui	69,000 ADSs	\$58.00

If GSK is ranked at the median of the performance comparator group, 35% of the shares will vest. Any ranking below this point will result in no shares vesting. Only if GSK is one of the top two companies will all of the shares vest. When determining vesting levels, the Committee has regard for the company's underlying financial performance.

The table below sets out the vesting schedule for the 2007 awards based on a performance comparator group comprising 14 companies excluding GSK.

TSR rank	Percentage of award vesting*
1	100%
2	100%
3	90%
4	80%
5	70%
6	60%
7	50%
Median	35%
Below median	0%

* TSR is measured on a pro-rata basis. Where GlaxoSmithKline's performance falls between two of the comparators, the level of vesting will be determined by the actual relative level of TSR rather than simple ranking.

To provide a closer link between shareholder returns and payments to the Executives, notional dividends are reinvested and paid out in proportion to the vesting of the award. The receipt of dividends has been incorporated into the benchmarking of award levels. In addition, performance shares earned by the Executives cannot be sold, except to meet related tax liabilities, for a further two years following the end of the vesting period. The Committee believes that this further aligns the interests of the Executives with the long-term interests of shareholders.

The Performance Share Plan awards granted in December 2003, with the performance period starting on 1st January 2004 and ending on 31st December 2006 did not vest for the Executives who were in office in 2003 because GSK's relative TSR performance was below the median and as a result the awards lapsed.

The awards made in 2003 to other senior executives, including Dr Slaoui and Mr Heslop, were dependent in part on TSR performance and in part on EPS performance. Half of these awards vested as GSK's EPS performance reached the target level for full vesting.

The vesting tables for the performance share awards granted in 2003, 2004 and 2006 are given on page 80.

b) Share options

Share options allow a holder to buy shares at a future date at the share price prevailing at the time of grant. Share options are granted to more than 12,000 managers at GlaxoSmithKline, including the Executives. The vesting of the share options granted to the Executives is linked to the achievement of compound annual EPS growth over the performance period. EPS is measured at constant exchange rates (CER) as it is GSK's practice to measure performance on a CER basis.

The Committee considers that EPS is the key measure of the performance of the business and is fully reflected through the business measures extended throughout the Group, ensuring organisational alignment.

When setting EPS targets, the Committee considers prior to each grant, the company's internal projections and analysts' forecasts for GlaxoSmithKline's EPS performance, as well as analysts' forecasts for the pharmaceutical industry.

After extensive and careful consideration, the Committee agreed that the annualised growth in EPS to achieve 100% vesting for the share option awards granted in February 2007 would be RPI + 6%.

The following key principles govern the use of EPS as a performance measure:

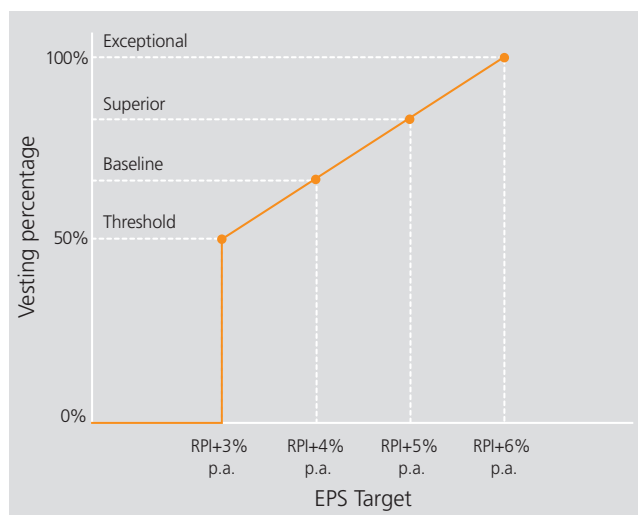
- adjustments will only be considered for major items
- adjustments will be for the judgement of the Committee
- the purpose of the adjustments is to ensure that the performance measurement is fair and reasonable to both participants and shareholders
- any discretion exercised by the Committee will be disclosed to shareholders in the Annual Report.

The Committee will set out the basis of its decision if it considers it appropriate to make any adjustment.

The table below sets out the share option awards made in February 2007, for which full disclosure will be made in the 2007 Remuneration Report.

Executive Director	Share option award	Option price
Dr Garnier	550,000 ADSs	\$58.00
Mr Heslop	242,750 shares	£14.88
Dr Slaoui	158,750 ADSs	\$58.00

For share option grants in 2007, vesting increases on a straight-line basis for EPS performance between the hurdles set out in the following graph.



This performance condition is substantially consistent with UK shareholder guidelines and expectations and is demanding when compared with those operated by other global pharmaceutical companies. This is consistent with the policy of providing pay for performance and only for performance.

Performance is measured over periods of three financial years. The performance period starts in the year of award with the base year being the preceding financial year. There is no performance retesting, so if the performance condition is not met after the three-year period the options will lapse.

The Share Options granted in 2003 vested in full.

Remuneration Report

continued

Pensions

The Executives participate in GlaxoSmithKline senior executive pension plans. The pension arrangements are structured in accordance with the plans operated for executives in the country in which the executives are likely to retire. Details of individual arrangements for the Executive Directors are set out on page 81. In response to the new pensions regime in the UK, the Committee carefully considered the impact of the change in legislation and decided the following:

- the company will continue to fulfil its obligations under existing pension arrangements
- no compensation will be provided if participants are adversely affected by the new pension regime.

The GSK pension policy for executives in the UK is:

- newly employed executives benefit from a company contribution of 15% of base pay under the defined contribution plan together with the opportunity to receive up to a further 4% in matched contributions
- legacy final salary plans which provide for two-thirds of final salary at age 60 were grandfathered for existing employees and no new entrants have been allowed
- for capped employees, benefits in excess of the cap are currently all provided through unfunded arrangements
- under the legacy final salary plans, actuarial reduction factors apply where a participant leaves employment of his own accord before the age of 60, effectively spreading the value of the pension earned over a longer life expectancy. If employment is terminated by the company (e.g. redundancy) the reduction factors will not apply.

In the USA, GSK operates a US cash balance plan which provides for an annual contribution and interest on the sum accumulated in the cash balance plan but with no contractual promise to provide specific levels of retirement income.

In light of market data, an extensive review of the pension arrangements for US executives was undertaken by the Committee during 2006. This review took account of the cost implications for the company as well as the competitiveness of the current arrangements. The conclusion was that the pension offered by GSK in the USA had fallen significantly behind the market at the senior level.

In view of this and taking account of concerns raised by both institutions and investors in relation to the basis on which contributions were previously determined under the US cash balance plan, the Committee approved the introduction of a new US executive cash balance plan. This change took effect from 1st January 2006 for senior US executives with the exception of the CEO, whose provisions were grandfathered in light of his anticipated retirement in 2008. Under this plan contributions are determined solely by reference to the executive's base salary. Contribution rates under the plan range from 15% to 38% of base salary. For capped employees in the USA benefits above the cap are provided by an unfunded non-qualified plan.

Share ownership requirements

To align the interests of executives with those of shareholders, executives are required to maintain significant holdings of shares in GlaxoSmithKline. These requirements are an important part of aligning the interests of executives with shareholders. The CEO is required to hold shares to the value of four times base salary. Other Executive Directors are required to build a shareholding to the value of three times base salary. Members of the CET are required to build a shareholding to a value of two times base salary. The other top 700 executives in the Group are required to build a shareholding to the value of one times base salary and are required to confirm this holding which is audited by KPMG on an annual basis.

In order for shares to qualify for these share ownership requirements they must be held personally by the Executive or their spouse (except where the spouse is also employed by GSK and is also subject to these requirements) or minor children or have been earned but deferred under one of the share programmes operated by the company. Unexercised share options are not included in this calculation.

As at 31st December 2006, Dr Garnier's holding was 497,545 ADSs, Dr Slaoui's was 114 ADSs and 42,815 ordinary shares and Mr Heslop's was 28,554 ordinary shares. Dr Garnier's holding was in excess of the share ownership requirements. Mr Heslop has until December 2008 and Dr Slaoui has until December 2009 to build their holdings to the value of three times base salary.

Executives are required to continue to satisfy these shareholding requirements for a minimum of twelve months following retirement from the company. Dr Yamada and Mr Coombe, who retired on 31st May 2006 and 31st March 2005 respectively, both met this requirement.

Other remuneration elements

The Executives participate in various legacy Glaxo Wellcome and SmithKline Beecham all-employee share plans in either the UK or the USA and in the GlaxoSmithKline plans that replaced them.

The Sharesave plan and the ShareReward plan are UK HM Revenue and Customs approved plans open to all UK employees on the same terms. Mr Heslop is a member of the Sharesave plan, into which he contributes £250 a month. This provides him with the option to buy shares at the end of the three-year savings period in line with the opportunity available to all UK employees.

Mr Heslop also contributes £125 per month to buy shares under the ShareReward plan. The company matches the number of shares bought each month.

The Executives also receive other benefits including healthcare (medical and dental), personal financial advice and life assurance. The cash value of the benefits received by the Executive Directors in 2006 is shown on page 73.

Executive Director terms, conditions and remuneration

Executive Director contracts

The policy set out below provides the framework for contracts for Executive Directors appointed since 2003 and going forward.

Aspect	Policy
Notice period on termination by the employing company or executive	12 calendar months
Termination payment	– 1x annual salary and 1x annual 'on-target' bonus ¹ – No mitigation required ²
Benefits	Governed by benefits policy, including: – healthcare (medical and dental) – personal financial advice – life assurance contributions
Vesting of long-term incentives	Rules of relevant equity incentive plan ³
Pension	Based on existing arrangements and terms of the relevant pension plan
Non-compete clause	12 months from termination notice date ²

¹ Dr Garnier's target bonus is 100% of salary, Dr Slaoui's is 85% of salary and Mr Heslop's is 75% of salary. When reviewing the level of severance payments, the Committee considered investor and DTI guidance. However, it determined that in line with competitive practice it is appropriate to provide for the payment of salary and target bonus on termination.

² The imposition of a 12-month non-compete period on the Executives is considered vitally important by the company in order to protect the Group's intellectual property. In light of the non-compete clause and competitor practice, the Committee believes that it would not be appropriate to provide for mitigation in the contracts.

³ As approved by shareholders of GlaxoSmithKline, Glaxo Wellcome and SmithKline Beecham, as appropriate.

In 2003, Dr Garnier agreed to changes to his previous contractual terms without compensation to come broadly in line with the new contractual framework, including the reduction of contractual notice period from 24 to 12 calendar months. However, in order to honour certain aspects of his 'old' contractual terms, there are a number of individual features which were retained.

These include the entitlement to reimbursement of excise tax on change of control related payments and, life insurance benefit funded by the company to age 65.

In relation to LTI awards, these are subject to performance testing, and any options or performance share awards made within 12 months of the termination notice date will lapse. However, on termination by the company (other than for cause), on retirement or on resignation for 'good reason' (i.e. resignation due to not being elected or retained as a director of the company or any merged company, or as a result of a change of control provided that such resignation occurs on or within 30 days of the first anniversary of the change in control) options remain exercisable for the full option term.

In addition, Dr Garnier is entitled to receive one year's worth of pension contributions on termination.

The following table sets out the details of the Executive Directors' service contracts:

Current Directors	Date of contract	Effective date	Expiry date
Dr Garnier	03.03.04	01.01.04	31.05.08
Mr Heslop	16.03.05	01.04.05	31.01.14
Dr Slaoui	16.05.06	01.06.06	01.08.19

Former Directors	Date of contract	Effective date	Expiry date
Dr Yamada*	27.07.04	01.01.04	30.06.07
Mr Coombe	03.03.04	01.01.04	31.03.05

* Dr Yamada retired from the Board and the company on 31st May 2006.

No termination payments will be made in respect of any part of a notice period extending beyond the contract expiry dates.

Individual pension arrangements

For individual pension arrangements for the Executive Directors refer to page 81.

Other entitlements

In addition to the contractual provisions outlined above, in the event that Executive Directors' service agreements are terminated by their employing company, the following would apply:

- in the case of outstanding awards under the GlaxoSmithKline Annual Investment Plan, provided that their agreement is terminated other than for cause, any deferred amount, and any income and gains, are automatically distributed as soon as administratively practicable after termination. If they resign, retire or the termination is for cause, then any deferred amount is not distributed until the end of the minimum three-year deferral period
- in line with the policy applicable to US senior executives, Dr Garnier and Dr Yamada are entitled to receive continuing medical and dental insurance. Dr Slaoui is a member of the same plan and may become eligible, at a future date, to receive continuing medical and dental cover into retirement
- following the merger, those participants in the legacy share option schemes who elected to exchange their legacy options for options over GlaxoSmithKline shares will receive an additional cash benefit equal to 10% of the grant price of the original option. This additional benefit is triggered when the new option is exercised or lapses. To qualify for this additional cash benefit, participants had to retain their options until at least the second anniversary of the effective date of the merger.

Outside appointments for Executive Directors

Any outside appointments must be approved by the Chairman on behalf of the Board. It is the company's policy that remuneration earned from such appointments may be kept by the individual Executive Director.

Remuneration Report

continued

Non-Executive Director terms, conditions and fees

Non-Executive Directors of GlaxoSmithKline do not have service contracts but instead have letters of appointment under which it is agreed that they serve the company as a Non-Executive Director until the conclusion of the Annual General Meeting following the third anniversary of their appointment. In each case this can be extended for a further term of three years by mutual agreement. No Directors serve a term longer than three years without offering themselves for re-election by the shareholders. The company aims to provide Non-Executive Directors with fees that are competitive with other companies of equivalent size and complexity.

The following table shows the date of the initial letter of appointment of each Non-Executive Director:

Non-Executive Director	Date of letter of appointment
Dr S Burns	12.02.07
Mr L Culp	09.06.03
Sir Crispin Davis	09.06.03
Sir Deryck Maughan	26.05.04
Dr D Podolsky	03.07.06
Sir Ian Prosser	19.06.00
Dr R Schmitz	19.06.00
Mr T de Swaan	21.12.05
Sir Robert Wilson	09.06.03

The fee structure for the Non-Executive Directors is as follows:

	Per annum
Standard annual cash retainer fee	£60,000

Supplemental fees

Senior Independent Director, the Audit Committee Chairman and Scientific/Medical Experts	£30,000
Chairmen of the Remuneration and Corporate Responsibility Committees	£20,000

Non-Executive Director undertaking intercontinental travel to meetings	£5,000 per meeting
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Exchange rate

Fees that are paid in US dollars are converted at a rate of £1/US\$1.8162, being the exchange rate that applied on 29th July 2004 when the new fee arrangements were approved by the Board.

Non-Executive Directors' share allocation plan

To enhance the link between Directors and shareholders GlaxoSmithKline requires Non-Executive Directors to receive a significant part of their fees in the form of shares. At least 25% of the Non-Executive Directors' total fees, excluding the Chairman, are paid in the form of shares or ADSs and allocated to a share account. The Non-Executive Directors may also take the opportunity to invest part or all of the balance of their fees into the same share account.

The shares or ADSs which are notionally awarded to the Non-Executive Directors and allocated to their interest accounts are included within the Directors' interests tables on page 76. The accumulated balance of these shares or ADSs, together with notional dividends subsequently reinvested, are not paid out to the Non-Executive Directors until retirement. Upon retirement, the Non-Executive Directors will receive either the shares or ADSs or a cash amount equal to the value of the shares or ADSs at the date of retirement.

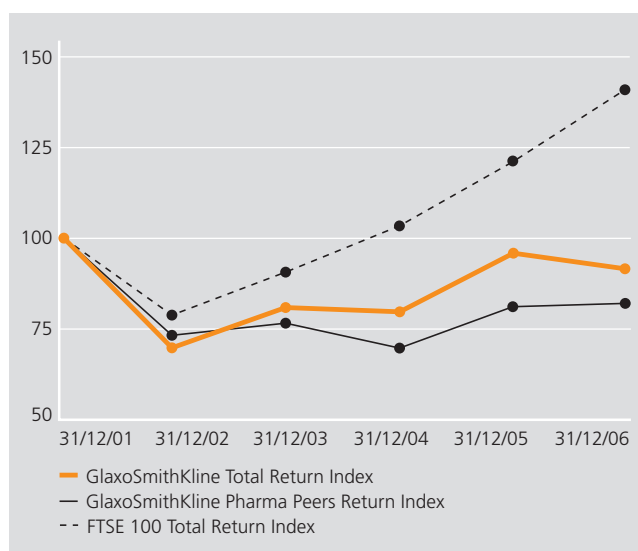
Non-Executive Directors are not entitled to compensation if their appointment is terminated.

Chairman

Sir Christopher Gent's letter of appointment to the Board was dated 26th May 2004, under which it was agreed that he serve the company as Deputy Chairman until 31st December 2004 and from 1st January 2005 as Chairman until the conclusion of the Annual General Meeting following the third anniversary of his appointment. This may be extended for a further term of three years by mutual agreement. In 2006, he received £400,000 per annum plus an allocation of GlaxoSmithKline shares to the value of £100,000 per annum as Chairman. Following a review, the Board agreed to increase his fees with effect from 1st January 2007, to £460,000 per annum plus an allocation of GlaxoSmithKline shares to the value of £115,000 per annum.

TSR performance graph

The following graph sets out the performance of the company relative to the FTSE 100 Index of which the company is a constituent and to the performance comparator group from 1st January 2002 to 31st December 2006. The graph has been prepared in accordance with the Regulations and is not an indication of the likely vesting of awards granted under any of the company's incentive plans.



Directors and Senior Management remuneration

The following tables set out for the Directors of GlaxoSmithKline plc the remuneration earned in 2006, their interests in shares of GlaxoSmithKline plc, their interests in share options and incentive plans and their pension benefits. The members of the CET and the Company Secretary, known as the Senior Management, also participate in the same remuneration plans as the Executive Directors and the aggregate remuneration and interests of the Directors and Senior Management are also provided.

Annual remuneration

	Footnote	2006				2005				
		Fees and salary 000	Other benefits 000	Annual bonus 000	Total annual remuneration 000	Fees and salary 000	Other benefits 000	Annual bonus* 000	Deferred bonus 000	Total annual remuneration 000
Executive Directors										
Dr JP Garnier	a,b,c	\$1,700	\$633	\$3,080	\$5,413	\$1,582	\$641	\$2,812	\$1,556	\$6,591
Dr M Slaoui		\$370	\$317	\$497	\$1,184	–	–	–	–	–
Mr J Heslop		£380	£31	£437	£848	£240	£9	£280	–	£529
Non-Executive Directors										
Sir Crispin Davis		£70	–	–	£70	£70	–	–	–	£70
Sir Christopher Gent		£500	£1	–	£501	£500	–	–	–	£500
Sir Ian Prosser		£95	–	–	£95	£100	–	–	–	£100
Dr R Schmitz		£90	–	–	£90	£95	–	–	–	£95
Mr T de Swaan		£70	–	–	£70	–	–	–	–	–
Sir Robert Wilson		£90	–	–	£90	£90	–	–	–	£90
Mr L Culp		\$136	–	–	\$136	\$136	–	–	–	\$136
Sir Deryck Maughan		\$136	–	–	\$136	\$146	–	–	–	\$146
Dr D Podolsky		\$100	–	–	\$100	–	–	–	–	–
Former Directors										
Mr J Coombe	c,d	–	£22	–	£22	£139	£32	–	–	£171
Dr M Barzach	e	£57	–	–	£57	£58	–	–	–	£58
Sir Roger Hurn		–	–	–	–	–	£5	–	–	£5
Sir Peter Job		–	–	–	–	–	£5	–	–	£5
Sir Richard Sykes		–	£1	–	£1	–	£1	–	–	£1
Dr T Yamada	a,b,c	\$428	\$493	\$281	\$1,202	\$763	\$739	\$1,110	\$698	\$3,310
Dr L Shapiro	f	\$144	\$11	–	\$155	\$230	–	–	–	\$230
Total Remuneration		£2,982	£841	£2,523	£6,346	£2,862	£810	£2,436	£1,238	£7,346
Analysed as:										
Executive Directors		£1,499	£545	£2,371	£4,415	£1,109	£361	£1,826	£855	£4,151
Non-Executive Directors		£1,116	£1	–	£1,117	£1,010	–	–	–	£1,010
Former Directors		£367	£295	£152	£814	£743	£449	£610	£383	£2,185
Total Remuneration		£2,982	£841	£2,523	£6,346	£2,862	£810	£2,436	£1,238	£7,346

Remuneration for Directors on the US Payroll is reported in Dollars. Dollar amounts are included in the totals based on conversion to Sterling at the average exchange rates for each year.

- Following the merger, and in order to encourage employees to convert their non-savings related options, held over Glaxo Wellcome or SmithKline Beecham shares or ADSs, for options over GlaxoSmithKline shares or ADSs, employees were granted an additional cash benefit equal to 10% of the grant price of the original option. This additional benefit, known as the Exchange Offer Incentive (EOI), is only payable when the new option is exercised or lapses above market value. To qualify for this additional cash benefit, participants had to retain these options until at least the second anniversary of the effective date of the merger. During the year, Dr Garnier received \$192,639 (2005 – \$174,472) and Dr Yamada received \$60,204 (2005 – \$167,405) relating to options exercised (page 78).
- Dr Garnier is a Non-Executive Director of United Technologies Corporation, in respect of which in 2006 he received \$230,000 in the form of deferred stock units. In 2005, Dr Garnier received \$110,000 in the form of deferred stock units and 3,000 stock options with a grant price of \$101.05. Dr Yamada is a member of the Advisory Board of Quaker BioVentures, Inc., for which, in the period from 1st January 2006 until his retirement from GlaxoSmithKline on 31st May 2006, he received \$5,000 (2005 – \$12,000).
- In 2001, following the merger, Dr Garnier, Mr Coombe and Dr Yamada were awarded a one-off special deferred bonus as members of the CET. Each was awarded an amount equivalent to his annual salary on 31st December 2001 and this was notionally invested in GlaxoSmithKline shares or ADSs on 15th February 2002 and deferred for three years. The deferred bonus vested on 15th February 2005 and the amounts paid were equivalent to the then value of GlaxoSmithKline shares or ADSs notionally acquired in February 2002 plus dividends reinvested over the period. Dr Garnier received \$1,556,324, and Dr Yamada received \$697,663. Mr Coombe waived his deferred bonus of £383,924. The company made a contribution to the pension plan in 2005 of £383,924 to enhance his pension entitlements. This amount is not included in the table above.
- Mr Coombe waived his prorated 2005 bonus of £106,870. The company made contributions to the pension plan in 2005 of £106,870 to enhance his pension entitlements. These amounts are not included within fees and salary above.
- Dr Barzach received fees of €84,244 (2005 – €84,244) from GlaxoSmithKline France for healthcare consultancy provided. These are included within fees and salary above.
- Although Dr Shapiro retired from the Board on 17th May 2006 she continues to be a member of GlaxoSmithKline's Scientific Advisory Board for which during 2006, she received fees of \$85,000 (2005 – \$85,000), of which \$30,000 (2005 – \$30,000) was in the form of ADSs. These are included within fees and salary above.

None of the above Directors received expenses during the year requiring separate disclosure as required by the Regulations.

Dr S Burns joined the Board as a Non-Executive Director on 12th February 2007, therefore no fees were paid to her in 2006.

* In light of the low take up levels and in response to concerns expressed by institutional investors in relation to the 1 for 10 non-performance related match provided under the Annual Investment Plan (AIP), the Committee decided in 2005 to discontinue the AIP. This was open to approximately 700 senior executives who all participated on the same terms. The last deferral elections under the AIP were made in respect to bonuses earned during 2005. Although the AIP has now closed, GSK will continue to manage the ongoing administration of subsisting awards as required by the AIP rules.

Remuneration Report

continued

Non-Executive Directors' remuneration

Fees	2006			2005		
	Total 000	Cash 000	Shares/ADSs 000	Total 000	Cash 000	Shares/ADSs 000
Current Non-Executive Directors						
Sir Crispin Davis	£70	–	£70	£70	–	£70
Sir Christopher Gent	£500	£400	£100	£500	£400	£100
Sir Ian Prosser	£95	£48	£47	£100	£50	£50
Dr R Schmitz	£90	£54	£36	£95	£57	£38
Mr T de Swaan	£70	£53	£17	–	–	–
Sir Robert Wilson	£90	£68	£22	£90	£68	£22
Mr L Culp	\$136	–	\$136	\$136	–	\$136
Sir Deryck Maughan	\$136	–	\$136	\$146	–	\$146
Dr D Podolsky	\$100	\$50	\$50	–	–	–
Former Non-Executive Directors						
Dr L Shapiro	\$59	\$52	\$7	\$145	\$109	\$36
Total Remuneration	£1,148	£678	£470	£1,090	£635	£455

The table above sets out the remuneration received as Non-Executive Directors of GlaxoSmithKline. Accordingly, it does not include Dr Shapiro's fees received as a member of GlaxoSmithKline's Scientific Advisory Board.

From the formation of GSK, the Non-Executive Directors have been required to take at least a part of their total fees in the form of shares allocated to a share account. At least 25% of Non-Executive Directors fees, except those of the Chairman (see page 72 for further details) must be taken under the fee allocation arrangement. Non-Executive Directors can then elect to receive either all or part of the remaining cash payment in the form of further shares or ADSs. The total value of these shares and ADSs as at the date of award, together with the cash payment, forms their total fees, which are included within the Annual remuneration table under 'Fees and salary'. The table above sets out the value of their fees received in the form of cash and shares and ADSs.

The table below sets out the accumulated number of shares and ADSs held by each Non-Executive Director in relation to their fees received as Board members as at 31st December 2006, together with the movements in their account over the year.

Non-Executive Directors' share arrangements	Footnote	Number of shares and ADSs				
		At 31.12.05	Elected	Dividends reinvested	Paid out	At 31.12.06
Current Non-Executive Directors						
Shares						
Sir Crispin Davis		12,758	4,839	460	–	18,057
Sir Christopher Gent		10,386	6,952	383	–	17,721
Sir Ian Prosser		16,590	3,295	580	–	20,465
Dr R Schmitz		13,898	2,477	487	–	16,862
Mr T de Swaan		–	1,226	7	–	1,233
Sir Robert Wilson		3,047	1,557	112	–	4,716
ADSs						
Mr L Culp		6,227	2,552	200	–	8,979
Sir Deryck Maughan		4,242	2,552	139	–	6,933
Dr D Podolsky		–	942	–	–	942
Former Non-Executive Directors						
Shares						
Dr L Shapiro	a	1,723	–	40	–	1,763
Sir Roger Hurn	b	10,284	–	–	(10,284)	–
ADSs						
Dr L Shapiro	a	3,426	130	73	–	3,629

Dividends are notionally reinvested at the end of the financial year in which payment is made.

The table below sets out the settlement of former Non-Executive Directors' share arrangements on their leaving the Board:

		Date of leaving	Value of awards on allocation	Value of awards on leaving	Payments in 2006
Current year					
Dr L Shapiro	a,c	17.05.06	\$196,673	\$259,163	\$259,163
Prior years					
Sir Roger Hurn	b	05.06.03	–	–	£151,948

a) Dr Shapiro's closing balance appears as at 17th May 2006, the date when she left the Board. All share arrangements with Dr Shapiro were settled in September 2006 with a lump sum cash payment.

b) On leaving the Board, Sir Roger Hurn elected to receive the settlement of his Non-Executive Directors' share arrangements in 40 quarterly cash payments. In July 2006, Sir Roger agreed to receive the outstanding balance of this plan as a lump sum.

c) The change in value of awards between allocation and leaving is attributable to dividends re-invested and the change in share price between the dates of award and the dates of leaving.

Remuneration Report

continued

Directors' interests

The following beneficial interests of the Directors of the company are shown in the register maintained by the company in accordance with the Companies Act 1985:

	Footnote	Shares			ADSs		
		23rd February 2007	31st December 2006	1st January 2006	23rd February 2007	31st December 2006	1st January 2006
Executive Directors							
Dr JP Garnier	a	–	–	–	251,124	250,528	225,896
Dr M Slaoui	b	39,659	36,955	38,821	156	114	–
Mr J Heslop	c	41,331	28,554	18,885	–	–	–
Non-Executive Directors							
Dr S Burns	d	44	–	–	95	–	–
Mr L Culp	e	–	–	–	8,979	8,979	6,227
Sir Crispin Davis	e	23,224	23,224	17,925	–	–	–
Sir Christopher Gent	e	17,721	17,721	10,386	–	–	–
Sir Deryck Maughan	e	–	–	–	6,933	6,933	4,242
Dr D Podolsky	e,f	–	–	–	942	942	–
Sir Ian Prosser	e	21,375	21,375	17,500	–	–	–
Dr R Schmitz	e	22,542	22,542	13,898	–	–	2,840
Mr T de Swaan	e	1,233	1,233	–	–	–	–
Sir Robert Wilson	e	5,844	5,844	4,175	–	–	–
Former Directors							
Dr T Yamada	a,g	–	–	–	–	73,912	67,512
Dr L Shapiro	e,g	–	1,763	1,723	–	7,900	7,401

One GlaxoSmithKline ADS represents two GlaxoSmithKline shares.

- a) Includes the equivalent number of ADSs purchased in the GlaxoSmithKline Stock Fund within the 401(k) plan.
- b) In the case of Dr Slaoui, the opening number of shares is shown as at 17th May 2006.
- c) Includes shares purchased through the GlaxoSmithKline ShareReward Plan for Mr Heslop totalling 1,250 at 31st December 2006 (31st December 2005 – 1,013) and 1,295 shares at 23rd February 2007.
- d) Dr Burns joined the Board on 12th February 2007.
- e) Includes shares and ADSs received as part or all of their fees as described under Non-Executive Directors' share arrangements on page 72. Dividends received on these shares and ADSs were converted to shares and ADSs as at 31st December 2006. These are also included in the Directors' interests above.
- f) Dr Podolsky joined the Board on 1st July 2006 and did not own any shares in GlaxoSmithKline at that date.
- g) Dr Yamada left the Board on 31st May 2006 and Dr Shapiro left the Board on 17th May 2006. Therefore their closing interests are recorded in the table above at these dates and are not included at 23rd February 2007.

The interests of the above-mentioned Directors at 23rd February 2007 reflect the change between year-end and that date.

Share options

Options – Shares

	Footnote	At 31.12.05	Date of grant	Exercise period	Grant price	Granted		At 31.12.06
						Number	Exercised	
Dr M Slaoui	a,b	170,712	–	–	–	–	–	170,712
Mr J Heslop	a	365,504	21.02.06	21.02.09 – 20.02.16	£14.68	231,000	54,000	542,504

Options – ADSs

	Footnote	At 31.12.05	Date of grant	Exercise period	Grant price	Granted		At 31.12.06
						Number	Exercised	
Dr JP Garnier	a	3,765,594	21.02.06	21.02.09 – 20.02.16	\$51.02	500,000	68,411	4,197,183
Dr T Yamada	c	1,148,490	–	–	–	–	21,380	1,127,110

- a) As part of the main option grant that occurred on 20th February 2007, with a vesting period of 20th February 2007 to 20th February 2010, Dr Garnier and Dr Slaoui were awarded 550,000 and 162,320 ADS options respectively with a grant price of \$58.00. As part of the same grant Mr Heslop was awarded 242,750 share options with a grant price of £14.88.
- b) Dr Slaoui joined the Board on 17th May 2006. These details cover the period from 17th May 2006 to 31st December 2006 and include the interests of his wife who is also an employee of GSK.
- c) Dr Yamada retired on 31st May 2006 and as such was excluded from the grant of options on 21st February 2006, as he retired from the company within 12 months of the date of the grant. These details cover the period from 1st January 2006 to 31st May 2006. Dr Yamada's unvested awards will vest at the end of the relevant performance period, subject to performance.

For those options outstanding at 31st December 2006, the earliest and latest vesting and lapse dates for those above and below the market price for a GlaxoSmithKline share at the year end are given in the table below.

		Weighted average grant price	Number	Vesting date		Lapse date	
				earliest	latest	earliest	latest
Dr JP Garnier							
Above market price ("underwater") at year end:	vested options	\$59.46	1,133,448	23.11.01	24.11.02	22.11.08	23.11.09
Below market price at year end:	vested options	\$45.18	2,103,735	24.03.00	15.12.06	23.03.07	14.12.13
	unvested options	\$47.53	960,000	02.12.07	21.02.09	01.12.14	20.02.16
Total ADS options as at 31st December 2006		\$49.57	4,197,183				

		Weighted average grant price	Number	Vesting date		Lapse date	
				earliest	latest	earliest	latest
Dr M Slaoui							
Above market price ("underwater") at year end:	vested options	£18.56	15,522	24.11.02	24.11.02	23.11.09	23.11.09
	unvested options	£14.68	73,340	21.02.09	21.02.09	20.02.16	20.02.16
Below market price at year end:	vested options	£11.79	52,800	03.12.05	03.12.05	02.10.12	02.10.12
	unvested options	£11.23	29,050	02.12.07	02.12.07	01.12.14	01.12.14
Total share options as at 31st December 2006		£13.55	170,712				

This includes those share options held by Dr Slaoui's wife, who is also an employee of GSK.

		Weighted average grant price	Number	Vesting date		Lapse date	
				earliest	latest	earliest	latest
Mr J Heslop							
Above market price ("underwater") at year end:	vested options	£17.04	194,438	31.07.01	28.11.04	30.07.08	27.11.11
	unvested options	£14.68	231,000	21.02.09	21.02.09	21.02.16	21.02.16
Below market price at year end:	vested options	£12.70	54,000	28.10.06	28.10.06	26.10.13	26.10.13
	unvested options	£11.23	63,066	03.12.07	27.10.08	01.12.14	26.10.15
Total share options as at 31st December 2006		£14.93	542,504				

		Weighted average grant price	Number	Vesting date		Lapse date	
				earliest	latest	earliest	latest
Dr T Yamada							
Above market price ("underwater") at year end:	vested options	\$60.91	320,519	15.03.02	24.11.02	31.05.08	31.05.08
Below market price at year end:	vested options	\$47.02	530,591	13.11.00	03.12.05	12.11.07	31.05.08
	unvested options	\$44.15	276,000	01.06.06	01.06.06	31.05.08	01.12.08
Total ADS options as at 31st May 2006		\$50.27	1,127,110				

The lapse dates for Dr Yamada's options have been modified to reflect his retirement in 2006.

Remuneration Report

continued

GSK grants share options to Executive Directors and Senior Managers on an annual basis. The Directors hold these options under the various share option plans referred to in Note 40 to the financial statements, 'Employee share schemes'. None of the other Directors had an interest in any option over the company's shares.

The table below sets out, for grants of share options in respect of the last four financial years, the grant year, the performance period, whether or not the options have vested, and the performance targets.

Grant	Performance period	Vesting status	Performance target	
			Annualised growth in EPS	Percentage of award vesting
November 2002	01.01.03 - 31.12.05	Vested	≥ RPI + 5%	100%
			RPI + 4%	75%
			RPI + 3%	50%
			< RPI + 3%	0%
December 2003	01.01.04 - 31.12.06	Vested	≥ RPI + 5%	100%
			RPI + 4%	75%
			RPI + 3%	50%
			< RPI + 3%	0%
December 2004	01.01.05 - 31.12.07	Not yet vested	≥ RPI + 5%	100%
			RPI + 4%	75%
			RPI + 3%	50%
			< RPI + 3%	0%
February 2006	01.01.06 - 31.12.08	Not yet vested	≥ RPI + 6%	100%
			RPI + 5%	83%
			RPI + 4%	67%
			RPI + 3%	50%
			< RPI + 3%	0%

Following the introduction of International Financial Reporting Standards (IFRS) on 1st January 2005, the Committee considered what EPS measurement basis, either IFRS or UK GAAP, should be used for share awards having performance periods that straddled the IFRS conversion data. The Committee determined that UK GAAP would be used for the 2002 grant (performance period 1st January 2003 to 31st December 2005) as two out of the three years would be reported under UK GAAP, and thereafter IFRS would apply.

Options exercised	Date	Number	Grant price	Market price	2006	2005
					Gain	Gain
Dr JP Garnier	30.10.06	68,411	\$28.16	\$53.12	\$1,707,351	\$2,029,561
Mr J Heslop	27.04.06	54,000	£11.79	£15.41	£195,480	£5,665
Dr T Yamada	03.05.06	21,380	\$28.16	\$56.77	\$611,712	\$2,083,931
Aggregate gain on options exercised					£1,449,028	£2,265,825

Dr Slaoui did not exercise any options between 17th May 2006 and 31st December 2006.

At the average exchange rate for the year, the above gain made by Dr Garnier amounted to £922,893. An EOI benefit of \$192,639 (£104,129) was paid to Dr Garnier on exercise of these options. This benefit has been included in the table on page 73.

On 8th February 2007, Dr Garnier exercised a further 68,411 options with a grant price of \$32.09 (market price on date of exercise was \$55.81) giving rise to a gain of \$1,622,709 (£877,140). Dr Garnier also received \$219,531 (£118,665) in respect of the EOI benefit arising on the exercise of these options.

At the average rate for the year, the above gain made by Dr Yamada amounted to £330,655. An EOI benefit of \$60,204 (£32,543) was paid to Dr Yamada on the exercise of these options. This benefit has been included in the table on page 73.

The highest and lowest closing prices during the year ended 31st December 2006 for GlaxoSmithKline shares were £15.77 and £13.26, respectively. The highest and lowest prices for GlaxoSmithKline ADSs during the year ended 31st December 2006 were \$58.38 and \$50.15, respectively. The market price for a GlaxoSmithKline share on 31st December 2006 was £13.44 (31st December 2005 – £14.69) and for a GlaxoSmithKline ADS was \$52.69 (31st December 2005 – \$50.48). The prices on 23rd February 2007 were £14.50 per GlaxoSmithKline share and \$56.92 per GlaxoSmithKline ADS.

Incentive plans

Performance Share Plan (PSP) awards

Dr JP Garnier – ADSs

Performance period	Unvested at 31.12.05	Number granted in 2006	Market price on date of grant	Vested & deferred			Lapsed	Additional ADS by dividends reinvested	Unvested at 31.12.06	Number granted in 2007
				Number	Market price	Gain				
01.01.03 – 31.12.05	70,000	–	\$37.25	35,000	\$51.35	\$1,797,247	35,000	–	–	–
01.01.04 – 31.12.06	212,763	–	\$44.57	–	–	–	–	6,629	219,392	–
01.01.05 – 31.12.07	204,881	–	\$43.73	–	–	–	–	6,383	211,264	–
01.01.06 – 31.12.08	–	220,000	\$51.02	–	–	–	–	3,186	223,186	–
01.01.07 – 31.12.09	–	–	\$58.00	–	–	–	–	–	–	240,000

Dr Garnier held 73,323 deferred PSPs at year-end. The increase in this balance of 36,648 relates to dividends reinvested during the year of 1,648 and a further 35,000 PSPs which vested during the year that Dr Garnier elected to defer. The total value of the awards vesting during 2006 was \$1,797,247.

Dr M Slaoui – Shares and ADSs

Performance period	Unvested at 17.05.06	Number granted in 2006	Market price on date of grant	Vested & exercised			Lapsed	Additional shares by dividends reinvested	Unvested at 31.12.06	Number granted in 2007
				Number	Market price	Gain				
01.01.04 – 31.12.06	5,000	–	£12.70	–	–	–	–	–	5,000	–
01.01.05 – 31.12.07	13,559	–	£11.63	–	–	–	–	201	13,760	–
01.01.06 – 31.12.08	28,720	–	£14.68	–	–	–	–	427	29,147	–

Performance period	Unvested at 31.12.05	Number granted in 2006	Market price on date of grant	Vested & exercised			Lapsed	Additional ADS by dividends reinvested	Unvested at 31.12.06	Number granted in 2007
				Number	Market price	Gain				
01.01.07 – 31.12.09	–	–	\$58.00	–	–	–	–	–	–	70,570

This includes those PSPs held by Dr Slaoui's wife, who is also an employee of GSK.

Mr J Heslop – Shares

Performance period	Unvested at 31.12.05	Number granted in 2006	Market price on date of grant	Vested & exercised			Lapsed	Additional shares by dividends reinvested	Unvested at 31.12.06	Number granted in 2007
				Number	Market price	Gain				
01.01.03 – 31.12.05	5,000	–	£11.79	2,500	£14.65	£36,625	2,500	–	–	–
01.01.04 – 31.12.06	5,000	–	£12.70	–	–	–	–	–	5,000	–
01.01.05 – 31.12.07	15,885	–	£11.63	–	–	–	–	501	16,386	–
01.01.06 – 31.12.08	–	100,000	£14.68	–	–	–	–	1,487	101,487	–
01.01.07 – 31.12.09	–	–	£14.88	–	–	–	–	–	–	105,000

Dr T Yamada – ADSs

Performance period	Unvested at 31.12.05	Number granted in 2006	Market price on date of grant	Vested & exercised			Lapsed	Additional ADS by dividends reinvested	Unvested at 31.05.06*	Number granted in 2007
				Number	Market price	Gain				
01.01.03 – 31.12.05	20,000	–	\$37.25	10,000	\$51.35	\$513,500	10,000	–	–	–
01.01.04 – 31.12.06	63,829	–	\$44.57	–	–	–	–	1,049	64,878	–
01.01.05 – 31.12.07	61,464	–	\$43.73	–	–	–	–	1,010	62,474	–

*Dr Yamada's unvested awards will vest at the end of the relevant performance period, subject to performance.

At the average exchange rate for the year, the above gains by Dr Garnier and Dr Yamada amounted to £971,485 and £277,567 respectively. The total gain on vesting of PSP awards made by Executive Directors is £1,285,677 (2005 – £1,431,804). The PSP is a medium-term incentive scheme introduced during 2001.

Under the terms of the PSP the number of shares actually vesting is determined following the end of the relevant three-year measurement period and is dependent on GSK's performance during that period as described on pages 68 and 69. The share awards were previously granted annually in November or December prior to the start of the performance period, but since the 2006 grant they are granted in February of the first year of performance period.

The measurement period commences on 1st January ending after three years on 31st December. For awards with a performance period commencing on 1st January 2005 and subsequent awards, dividends are reinvested on the PSPs awarded to members of the CET. Dividends are reinvested in the quarter in which payment is made. Under the terms of the PSP, US participants may defer receipt of all or part of their vested awards.

The PSP awards granted in December 2003, with the performance period starting on 1st January 2004 and ending on 31st December 2006 did not vest for the Executives who were in office in 2003 because GSK's relative TSR performance was below the median and as a result the awards lapsed. The awards made in 2003 to other senior executives, including Dr Slaoui and Mr Heslop, were dependent in part on TSR performance and in part on EPS performance. Half of these awards vested as GSK's EPS performance reached the target level for full vesting.

Remuneration Report

continued

The following vesting schedules apply to awards made in 2003, 2004 and 2006.

Award	Performance Period	Vesting schedule	
		TSR rank with 14 companies*	Percentage of award vesting**
2003	1st January 2004 to 31st December 2006	1	100%
2004	1st January 2005 to 31st December 2007	2	100%
		3	90%
		4	80%
		5	70%
		6	60%
		7	50%
		Median	35%
		Below median	0%

Award	Performance Period	Vesting schedule	
		TSR rank with 13 companies	Percentage of award vesting**
2006	1st January 2006 to 31st December 2008	1	100%
		2	100%
		3	87%
		4	74%
		5	61%
		6	48%
		Median	35%
		Below median	0%

* The performance comparator group for these awards comprised 14 other companies and GlaxoSmithKline. Both Aventis and Sanofi-Synthelabo were in the comparator group prior to their merger to form Sanofi-Aventis. For the purposes of calculating TSR over the performance period for the awards granted in December 2003, the starting price of the shares of the two individual companies will be compared to the price of the merged company at the end of the performance period, adjusted by the merger ratio. Dividends will be treated as having been reinvested during the performance period.

** TSR is measured on a pro-rata basis. Where GlaxoSmithKline's performance falls between two of the comparators, the level of vesting will be determined by the actual relative level of TSR rather than simple ranking.

Share Value Plan awards

Dr M Slaoui – Shares and ADSs

Plan year	Unvested at 17.05.06	Number granted in 2006	Market price on date of grant	Vested & exercised			Unvested at 31.12.06	Number of ADSs granted in 2007
				Number	Market price	Gain		
2004	4,660	–	£11.23	–	–	–	4,660	–
2006	1,200	–	£14.68	–	–	–	1,200	–
2007	–	–	\$58.00	–	–	–	–	890

In his capacity as SVP, Worldwide Business Development, Dr Slaoui was eligible to participate in the GSK Share Value Plan. Both Dr Slaoui and his wife, an employee of GSK, received awards under the Share Value Plan. Following the announcement of his appointment to the Board, in February 2006, he ceased to be eligible to receive awards under this plan. The awards are subject to a 3-year vesting period and the vesting is contingent on their continued employment with GSK.

Mid-Term Incentive Plan – ADSs

	Vested and deferred participations at 31.12.05	Additional ADS by dividends reinvested in 2006	Vested and deferred participations at 31.12.06
Dr JP Garnier	168,464	5,230	173,694

The Mid-Term Incentive Plan (MTIP) was a share award scheme operated by SmithKline Beecham. The plan closed to new entrants upon completion of the merger and no further participations have been granted.

Where a final award of ADSs is made, receipt of the award may be deferred by a Director. Dr Garnier deferred receipt of the full amounts vested in 1999, 2000, 2001, 2002 and 2003. The deferred awards, together with any additional ADSs subsequently received through dividend reinvestment, are not included in the Directors' interests table on page 76 since they are retained in the MTIP until paid out.

Stock Appreciation Rights (SARs) – ADSs	At 31.12.05	At 17.05.06	Average grant price
Dr L Shapiro	872	872	\$57.25

Dr Shapiro did not exercise any SARs in 2006. Her gain on exercise in 2005 was \$6,380.

All SARs held by Dr Shapiro had a grant price above the market price of a GlaxoSmithKline ADS at 17th May 2006, the date she retired from the Board of GlaxoSmithKline.

Dr Shapiro is a member of GlaxoSmithKline's Scientific Advisory Board (SAB). Dr Shapiro was a member of SmithKline Beecham's SAB from 1993 until the completion of the merger with Glaxo Wellcome. Along with other members of the SAB, she received annual grants of SmithKline Beecham SARs which, in general, vested three years from the date of grant and will expire 10 years from the date of grant. Grants of SARs to SAB members ceased in 1999.

SARs entitle the holder to a cash sum at a future date based on share price growth between the date of grant and the date of exercise.

Full provision is made in the financial statements for accrued gains on SARs from the date of grant. In connection with the merger, all previously granted SARs became immediately exercisable.

Pensions

The accrued annual pension benefits and transfer values for Executive Directors on retirement are set out below.

The regulations require disclosure of the accrued benefit at the end of the year, the change in accrued benefit over the year, the transfer value at both the beginning and end of the year, and the change in the transfer value over the year. The Listing Rules require additional disclosure of the change in the accrued benefit net of inflation and the transfer value of this change. Pensions for the Executive Directors have been disclosed in the currency in which the pension is payable.

	Accrued benefit at 31.12.05 000	Accrued benefit at 31.12.06 000	Change in accrued benefit over year 000	Personal contributions made to the scheme during the year 000	Transfer value at 31.12.05 000	Transfer value at 31.12.06 000	Change in transfer value* 000	Change in accrued benefit over year net of inflation 000	Transfer value of change in accrued benefit* 000
Current Executive Directors									
Dr JP Garnier	\$1,093	\$1,202	\$109	–	\$13,240	\$14,680	\$1,440	\$87	\$1,440
Dr M Slaoui	–	\$26	\$26	–	–	\$131	\$131	\$26	\$131
	€52	€53	€1	–	€493	€538	€45	–	€45
Mr J Heslop	£75	£111	£36	£11	£1,260	£1,930	£659	£34	£415
Former Executive Directors									
Dr T Yamada	\$168	\$169	\$1	–	\$1,985	\$2,110	\$125	–	\$125

*These are shown net of contributions made by the individual.

Dr Garnier is a member of the All Employee US Cash Balance Pension Plan, under which GlaxoSmithKline makes annual contributions calculated as a percentage of the employee's base salary and bonus. GlaxoSmithKline makes annual contributions of 15% of Dr Garnier's annual salary and bonus, as detailed in his contract. The fund increases at an interest rate set annually in advance based on the 30 year US treasury bond rate to provide a cash sum at retirement. This cash sum is used to purchase a pension at retirement based on the annuity rates applicable at that time. The plan has no entitlement to a spouse's pension or to pension increases, other than by reducing the executive's own initial pension.

The transfer value, or cash sum, of Dr Garnier's plan has increased by \$1,440,430 over the year as a result of further accumulation of interest and contributions paid by the company.

With effect from 1st June 2006, Dr Slaoui became a member of the US Executive Cash Balance Pension Plan, under which GlaxoSmithKline makes annual contributions calculated as a percentage of the executive's base salary. GlaxoSmithKline makes annual contributions of 38% of Dr Slaoui's annual salary. The fund increases at an interest rate set annually in advance based on the 30 year US treasury bond rate to provide a cash sum at retirement. This cash sum is used to purchase a pension at retirement based on the annuity rates applicable at that time. The plan has no entitlement to a spouse's pension or to pension increases, other than by reducing the executive's own initial pension.

Dr Slaoui was an active participant of the Belgium Fortes Plan until 31st May 2006. This plan is a defined benefit plan with a lump sum payable at Normal Retirement age for the plan which is 60 years of age. The transfer value, or cash sum, of Dr Slaoui's plan has increased by €45,042 over the year as a result of the further accumulation of interest and contributions paid by the company.

Mr Heslop participates in the Glaxo Wellcome Defined Benefit Plan with an accrual rate of 1/30th of final pensionable salary per annum. In 2000 all benefits accrued under the Glaxo Wellcome UK pension arrangements were augmented by the Trustees of the plans by 5% to reflect a distribution of surplus. This augmentation will apply to that element of Mr Heslop's pension earnings before 31st March 2000.

Remuneration Report

continued

Mr Heslop's transfer value has been calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11. The transfer value represents the present value of future payments to be made under the pension plan. Mr Heslop's annual accrued benefit has increased by £36,401 (£34,389 excluding the effects of inflation), and the transfer value less personal contributions has increased by £658,794 over the year. The increase in Mr Heslop's pensionable salary of £80,000 is the primary reason for the increase in transfer value.

Dr Yamada retired on 31st May 2006. He is a member of the All Employee US Cash Balance Pension Plan, under which GlaxoSmithKline makes annual contributions calculated as a percentage of the employee's base salary and bonus. GlaxoSmithKline made annual contributions of 18% of Dr Yamada's annual salary and bonus (as detailed in his contract). The fund increases at an interest rate set annually in advance based on the 30 year US treasury bond rate to provide a cash sum at retirement. This cash sum is used to purchase a pension at retirement based on the annuity rates applicable at that time. The plan has no entitlement to a spouse's pension or to pension increases, other than by reducing the executive's own initial pension. Dr Yamada commenced his pension benefit in the form of an annuity on 1st June 2006.

Dr Garnier, Dr Slaoui and Dr Yamada are also members of the US Retirement Savings Plan, a savings scheme open to all US employees and the Executive Supplemental Savings Plan, a savings scheme open to executives to restore US government limits imposed on the Retirement Savings Plan. Contributions to both plans are invested in a range of funds and the value of the accumulated funds is paid at retirement. During 2006, contributions of \$183,840 (£99,373) were paid into these two schemes by the company in respect of Dr Garnier. In respect of Dr Slaoui, contributions of \$20,354 (£11,002) were paid into the scheme. In respect of Dr Yamada, contributions of \$62,494 (£33,781) were paid into the scheme.

Directors and Senior Management

For US reporting purposes, it is necessary to provide information on compensation and interests of Directors and Senior Management as a group ('the group'). For the purpose, the group is defined as the Directors, members of the CET and the Company Secretary. For the financial year 2006, the total compensation paid to members of the group for the periods during which they served in that capacity was £14,906,027, the aggregate increase in accrued pension benefits, net of inflation, was £290,013 and the aggregate payment to defined contribution schemes was £446,115. During 2006, the group were granted 887,150 share options and 1,060,000 ADS options under the Share Option Scheme, 383,070 shares and 462,000 ADSs under the Performance Share Plan and were awarded 3,160 shares under the Share Value Plan. Members of the group were also awarded 21,339 shares and 38,458 ADSs through the reinvestment of dividends in the Performance Share Plan.

At 23rd February 2007, the group (comprising 25 persons) owned 573,400 shares and 346,738 ADSs, constituting less than 1% of the issued share capital of the company. The group also held, at that date: options to purchase 6,302,356 shares and 7,720,807 ADSs; 1,104,369 shares and 1,611,659 ADSs awarded under the Performance Share Plan, including those shares and ADSs that are vested and deferred; 222,403 vested and deferred ADSs under the legacy SmithKline Beecham Mid-Term Incentive Plan, and 21,020 shares and 3,850 ADSs awarded under the Share Value Plan. These holdings were issued under the various executive share option plans described in Note 40 to the financial statements, 'Employee share schemes'.

Directors' interests in contracts

Except as described in Note 33 to the financial statements, 'Related party transactions', during or at the end of the financial year no Director or connected person had any material interest in any contract of significance in relation to the Group's business with a Group company.

The Directors' Remuneration Report has been approved by the Board of Directors and signed on its behalf by

Sir Christopher Gent

Chairman

28th February 2007

Financial statements

This section comprises the Directors' statements of responsibility, the Independent Auditors' report on the financial statements and the consolidated financial statements consisting of the principal financial statements and supporting notes prepared under IFRS as adopted for use in the European Union. Also presented is the balance sheet of GlaxoSmithKline plc, which has been prepared under UK GAAP.

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Directors' statements of responsibility

Directors' statement of responsibility in relation to the consolidated financial statements

The Directors are responsible for:

- ensuring the maintenance of proper accounting records, which disclose with reasonable accuracy the financial position of the Group at any time and from which financial statements can be prepared to comply with the Companies Act 1985 and Article 4 of the IAS Regulation
- preparing financial statements for each financial period which give a true and fair view, in accordance with IFRS as adopted for use in the European Union, of the state of affairs of the Group as at the end of the financial period and of the profit or loss for that period
- ensuring the operation of systems of internal control and for taking reasonable steps to safeguard the assets of the Group and for preventing and detecting fraud and other irregularities.

The financial statements for the year ended 31st December 2006, comprising principal statements and supporting notes, are set out in 'Financial statements' on pages 86 to 164 of this report.

The Directors confirm that suitable accounting policies have been consistently applied in the preparation of the financial statements, supported by reasonable and prudent judgements and estimates as necessary.

The responsibilities of the auditors in relation to the financial statements are set out in the Independent Auditors' report (page 85 opposite).

The financial statements for the year ended 31st December 2006 are included in the Annual Report 2006, which is published in hard-copy printed form and made available on the website. The Directors are responsible for the maintenance and integrity of the Annual Report on the website in accordance with UK legislation governing the preparation and dissemination of financial statements. Access to the website is available from outside the UK, where comparable legislation may be different.

Disclosure of information to auditors

The Directors, in office at the date of this Report, have each confirmed that:

- so far as they are aware, there is no relevant audit information of which the company's auditors are unaware; and
- each Director has taken all the steps that he/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 234 ZA of the Companies Act 1985.

Directors' remuneration

The Remuneration Report on pages 65 to 82 sets out the remuneration policies operated by GlaxoSmithKline and disclosures on Directors' remuneration and other disclosable information relating to Directors and officers and their interests. It has been prepared in accordance with the Companies Act 1985 and complies with Section B of the Combined Code on Corporate Governance.

Going concern basis

After making enquiries, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

Internal control

The Board, through the Audit Committee, has reviewed the assessment of risks and the internal control framework that operates in GlaxoSmithKline and has considered the effectiveness of the system of internal control in operation in the Group for the year covered by this report and up to the date of its approval by the Board of Directors.

The Combined Code

The Board considers that GlaxoSmithKline plc applies the principles of the Combined Code on Corporate Governance of the Financial Reporting Council, as described under 'Corporate governance' on pages 53 to 63, and has complied with its provisions except as described on page 62.

As required by the Listing Rules of the Financial Services Authority, the auditors have considered the Directors' statement of compliance in relation to those points of the Combined Code which are specified for their review.

Annual Report

The Annual Report for the year ended 31st December 2006, comprising the Report of the Directors, the Remuneration Report, the Financial statements and additional information for investors, has been approved by the Board of Directors and signed on its behalf by

Sir Christopher Gent

Chairman

28th February 2007

Independent Auditors' report

to the members of GlaxoSmithKline plc

We have audited the Group financial statements of GlaxoSmithKline for the year ended 31st December 2006 which comprise the primary financial statements, the consolidated Income Statement, the consolidated Balance Sheet, the consolidated Cash Flow Statement, the consolidated Statement of Recognised Income and Expense and the related notes. These Group financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the parent company financial statements of GlaxoSmithKline for the year ended 31st December 2006 and on the information in the Directors' Remuneration Report that is described as having been audited.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the group financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' Responsibilities (page 84 opposite).

Our responsibility is to audit the Group financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the Group financial statements give a true and fair view and whether the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We also report to you whether in our opinion the information given in the Report of the Directors is consistent with the Group financial statements.

In addition we report to you if, in our opinion, we have not received all the information and explanations we require for our audit, or if information specified by law regarding director's remuneration and other transactions is not disclosed.

We review whether the Corporate Governance Statement reflects the company's compliance with the nine provisions of the Combined Code (2003) specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited Group financial statements. The other information comprises only the Financial summary, the Joint statement by the Chairman and Chief Executive, Financial trends and ratios, Business review and the Corporate governance statement.

We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Group financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Group financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the Group financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Group financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the Group financial statements.

Opinion

In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 31st December 2006 and of its profit and cash flows for the year then ended;
- the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation; and
- the information given in the Report of the Directors is consistent with the Group financial statements.

Separate opinion in relation to IFRSs

As explained in Note 1 to the Group financial statements, the Group in addition to complying with its legal obligation to comply with the IFRSs as adopted by the European Union, has also complied with the IFRSs as issued by the International Accounting Standards Board.

In our opinion the Group financial statements give a true and fair view, in accordance with IFRSs, of the state of the Group's affairs as at 31st December 2006 and of its profit and cash for the year then ended.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London
28th February 2007

Consolidated income statement

for the year ended 31st December 2006

	Notes	2006 £m	2005 £m	2004 £m
Turnover	5	23,225	21,660	19,986
Cost of sales		(5,010)	(4,764)	(4,360)
Gross profit		18,215	16,896	15,626
Selling, general and administration		(7,257)	(7,250)	(7,201)
Research and development		(3,457)	(3,136)	(2,904)
Other operating income	6	307	364	235
Operating profit	7,8	7,808	6,874	5,756
Finance income	9	287	257	176
Finance costs	10	(352)	(451)	(362)
Share of after tax profits of associates and joint ventures	11	56	52	60
Profit on disposal of interest in associates	36	–	–	149
Profit before taxation		7,799	6,732	5,779
Taxation	12	(2,301)	(1,916)	(1,757)
Profit after taxation for the year		5,498	4,816	4,022
Profit attributable to minority interests		109	127	114
Profit attributable to shareholders		5,389	4,689	3,908
		5,498	4,816	4,022
Basic earnings per share (pence)	13	95.5p	82.6p	68.1p
Diluted earnings per share (pence)	13	94.5p	82.0p	68.0p

Consolidated balance sheet

at 31st December 2006

	Notes	2006 £m	2005 £m
Non-current assets			
Property, plant and equipment	15	6,930	6,652
Goodwill	16	758	696
Other intangible assets	17	3,293	3,383
Investments in associates and joint ventures	18	295	276
Other investments	19	441	362
Deferred tax assets	12	2,123	2,214
Other non-current assets	20	721	438
Total non-current assets		14,561	14,021
Current assets			
Inventories	21	2,437	2,177
Current tax recoverable	12	186	416
Trade and other receivables	22	5,317	5,348
Liquid investments	30	1,035	1,025
Cash and cash equivalents	23	2,005	4,209
Assets held for sale	24	12	2
Total current assets		10,992	13,177
Total assets		25,553	27,198
Current liabilities			
Short-term borrowings	30	(718)	(1,200)
Trade and other payables	25	(4,871)	(5,147)
Current tax payable	12	(621)	(2,269)
Short-term provisions	27	(1,055)	(895)
Total current liabilities		(7,265)	(9,511)
Non-current liabilities			
Long-term borrowings	30	(4,772)	(5,271)
Deferred tax provision	12	(595)	(569)
Pensions and other post-employment benefits	26	(2,339)	(3,069)
Other provisions	27	(528)	(741)
Other non-current liabilities	28	(406)	(467)
Total non-current liabilities		(8,640)	(10,117)
Total liabilities		(15,905)	(19,628)
Net assets		9,648	7,570
Equity			
Share capital	31	1,498	1,491
Share premium account	31	858	549
Retained earnings	32	6,965	5,579
Other reserves	32	65	(308)
Shareholders' equity		9,386	7,311
Minority interests		262	259
Total equity		9,648	7,570

Approved by the Board on 28th February 2007

Sir Christopher Gent
Chairman

Consolidated cash flow statement

for the year ended 31st December 2006

	Notes	2006 £m	2005 £m	2004 £m
Cash flow from operating activities				
Cash generated from operations	34	8,203	7,665	6,527
Taxation paid		(3,846)	(1,707)	(1,583)
Net cash inflow from operating activities		4,357	5,958	4,944
Cash flow from investing activities				
Purchase of property, plant and equipment		(1,366)	(903)	(788)
Proceeds from sale of property, plant and equipment		43	54	53
Proceeds from sale of intangible assets		175	221	–
Purchase of intangible assets		(224)	(278)	(255)
Purchase of equity investments		(57)	(23)	(103)
Proceeds from sale of equity investments		32	35	58
Share transactions with minority shareholders	36	(157)	(36)	–
Purchase of businesses, net of cash acquired	36	(273)	(1,026)	(297)
Disposal of businesses and interest in associates	36	5	(2)	230
Investments in associates and joint ventures	36	(13)	(2)	(2)
Interest received		299	290	173
Dividends from associates and joint ventures		15	10	11
Net cash outflow from investing activities		(1,521)	(1,660)	(920)
Cash flow from financing activities				
(Increase)/decrease in liquid investments		(55)	550	(53)
Proceeds from own shares for employee share options		151	68	23
Issue of share capital	31	316	252	42
Share capital purchased for cancellation		–	–	(201)
Purchase of Treasury shares		(1,348)	(999)	(799)
Redemption of preference shares issued by subsidiary		–	–	(489)
Increase in long-term loans		–	982	1,365
Repayment of long-term loans		–	(70)	(15)
Net repayment of short-term loans		(739)	(857)	(407)
Net repayment of obligations under finance leases		(34)	(36)	(22)
Interest paid		(414)	(381)	(350)
Dividends paid to shareholders		(2,598)	(2,390)	(2,475)
Dividends paid to minority interests		(87)	(86)	(73)
Dividends paid on preference shares		–	–	(2)
Other financing cash flows		16	53	49
Net cash outflow from financing activities		(4,792)	(2,914)	(3,407)
(Decrease)/increase in cash and bank overdrafts	35	(1,956)	1,384	617
Exchange adjustments		(254)	233	(93)
Cash and bank overdrafts at beginning of year		3,972	2,355	1,831
Cash and bank overdrafts at end of year		1,762	3,972	2,355
Cash and bank overdrafts at end of year comprise:				
Cash and cash equivalents		2,005	4,209	2,467
Overdrafts		(243)	(237)	(112)
		1,762	3,972	2,355

Consolidated statement of recognised income and expense

for the year ended 31st December 2006

	2006 £m	2005 £m	2004 £m
Exchange movements on overseas net assets	(390)	203	(47)
Tax on exchange movements	(78)	99	(73)
Fair value movements on available-for-sale investments	84	(1)	–
Deferred tax on fair value movements on available-for-sale investments	(15)	(10)	–
Exchange movements on goodwill in reserves	31	9	6
Actuarial gains/(losses) on defined benefit plans	429	(794)	108
Deferred tax on actuarial movements in defined benefit plans	(161)	257	(17)
Fair value movements on cash flow hedges	(5)	(4)	–
Deferred tax on fair value movements on cash flow hedges	2	1	–
Net losses recognised directly in equity	(103)	(240)	(23)
Profit for the year	5,498	4,816	4,022
Total recognised income and expense for the year	5,395	4,576	3,999
Total recognised income and expense for the year attributable to:			
Shareholders	5,307	4,423	3,906
Minority interests	88	153	93
	5,395	4,576	3,999

Notes to the financial statements

1 Presentation of the financial statements

Description of business

GlaxoSmithKline is a major global healthcare group which is engaged in the creation and discovery, development, manufacture and marketing of pharmaceutical products, including vaccines, over-the-counter (OTC) medicines and health-related consumer products. GlaxoSmithKline's principal pharmaceutical products include medicines in the following therapeutic areas: central nervous system, respiratory, anti-virals, anti-bacterials, vaccines, oncology and emesis, metabolic, cardiovascular and urogenital.

Compliance with applicable law and IFRS

The financial statements have been prepared in accordance with the Companies Act 1985, Article 4 of the IAS Regulation and International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) and related interpretations, as adopted by the European Union.

For GSK, there are no differences between IFRS as adopted for use in the European Union and full IFRS as published by the International Accounting Standards Board.

Financial period

These financial statements cover the financial year from 1st January to 31st December 2006, with comparative figures for the financial years from 1st January to 31st December 2005 and, where appropriate, from 1st January to 31st December 2004.

Composition of the Group

A list of the subsidiary and associated undertakings which, in the opinion of the Directors, principally affected the amount of profit or the net assets of the Group is given in 'Principal Group companies', Note 42.

Composition of financial statements

The consolidated financial statements are drawn up in accordance with IFRS and with IFRS accounting presentation. The financial statements comprise:

- Consolidated income statement
- Consolidated balance sheet
- Consolidated cash flow statement
- Consolidated statement of recognised income and expense
- Notes to the financial statements.

Additional information in accordance with the requirements of US generally accepted accounting principles (US GAAP) is included in the notes to the financial statements. In Note 41 a statement of differences, and reconciliations of net income and shareholders' equity, between IFRS and US GAAP are provided.

Accounting convention

The financial statements have been prepared using the historical cost convention, modified for certain items carried at fair value, as stated in the accounting policies.

Accounting principles and policies

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

The financial statements have been prepared in accordance with the Group's accounting policies approved by the Board and described in Note 2.

Parent company financial statements

The financial statements of the parent company, GlaxoSmithKline plc, have been prepared in accordance with UK GAAP and with UK accounting presentation. The company balance sheet is presented on page 167.

2 Accounting policies

Information on the application of these accounting policies, including areas of estimation and judgement is given under 'Critical Accounting Policies' in 'Financial Review 2006' on page 37.

Consolidation

The consolidated financial statements include:

- the assets and liabilities, and the results and cash flows, of the company and its subsidiaries, including ESOP Trusts
- the Group's share of the results and net assets of associates and joint ventures.

The financial statements of entities consolidated are made up to 31st December.

Entities over which the Group has the power to govern the financial and operating policies are accounted for as subsidiaries. Where the Group has the ability to exercise joint control, the entities are accounted for as joint ventures, and where the Group has the ability to exercise significant influence, they are accounted for as associates.

Interests acquired in entities are consolidated from the date the Group acquires control and interests sold are de-consolidated from the date control ceases.

Transactions and balances between subsidiaries are eliminated; no profit before tax is taken on sales between subsidiaries or on sales to joint ventures and associates until the products are sold to customers outside the Group. Deferred tax relief on unrealised intra-Group profit is accounted for only to the extent that it is considered recoverable.

Goodwill arising on the acquisition of interests in subsidiaries, joint ventures and associates, representing the excess of the acquisition cost over the Group's share of the fair values of the identifiable assets, liabilities and contingent liabilities acquired, is capitalised as a separate item in the case of subsidiaries and as part of the cost of investment in the case of joint ventures and associates. Goodwill is denominated in the currency of the operation acquired. Where the cost of acquisition is below the fair value of the net assets acquired, the difference is recognised directly in the income statement.

The results and assets and liabilities of associates and joint ventures are incorporated into the consolidated financial statements using the equity method of accounting.

2 Accounting policies continued

Foreign currency translation

Foreign currency transactions are booked in the functional currency of the Group company at the exchange rate ruling on the date of transaction. Foreign currency monetary assets and liabilities are retranslated into local currency at rates of exchange ruling at the balance sheet date. Exchange differences are included in the income statement.

Assets and liabilities, including related goodwill, of overseas subsidiaries, associates and joint ventures, are translated into Sterling at rates of exchange ruling at the balance sheet date. The results and cash flows of overseas subsidiaries, associates and joint ventures are translated into Sterling using average rates of exchange. Exchange adjustments arising when the opening net assets and the profits for the year retained by overseas subsidiaries, associates and joint ventures are translated into Sterling, less exchange differences arising on related foreign currency borrowings which hedge the Group's net investment in these operations, are taken to a separate component of equity.

When translating into Sterling the assets, liabilities, results and cash flows of overseas subsidiaries, associates and joint ventures which are reported in currencies of hyper-inflationary economies, adjustments are made to reflect current price levels. Any loss on net monetary assets is charged to the consolidated income statement.

Revenue

Revenue is recognised in the income statement when goods or services are supplied or made available to external customers against orders received and when title and risk of loss passes to the customer. Turnover represents net invoice value after the deduction of discounts and allowances given and accruals for estimated future rebates and returns. The methodology and assumptions used to estimate rebates and returns are monitored and adjusted regularly in the light of contractual and legal obligations, historical trends, past experience and projected market conditions. Market conditions are evaluated using wholesaler and other third-party analyses, market research data and internally generated information. Turnover also includes co-promotion income where the Group records its share of the revenue but no related cost of sales. Value added tax and other sales taxes are excluded from revenue.

Expenditure

Expenditure is recognised in respect of goods and services received when supplied in accordance with contractual terms. Provision is made when an obligation exists for a future liability in respect of a past event and where the amount of the obligation can be reliably estimated. Manufacturing start-up costs between validation and the achievement of normal production are expensed as incurred. Advertising and promotion expenditure is charged to the income statement as incurred. Shipment costs on intercompany transfers are charged to cost of sales; distribution costs on sales to customers are included in selling, general and administrative expenditure. Restructuring costs are recognised in respect of the direct expenditure of a business reorganisation where the plans are sufficiently detailed and well advanced, and where appropriate communication to those affected has been undertaken.

Research and development

Research and development expenditure is charged to the income statement in the period in which it is incurred. Development expenditure is capitalised when the criteria for recognising an asset are met, usually when a regulatory filing has been made in a major market and approval is considered highly probable. Property, plant and equipment used for research and development is depreciated in accordance with the Group's policy.

Environmental expenditure

Environmental expenditure related to existing conditions resulting from past or current operations and from which no current or future benefit is discernible is charged to the income statement. The Group recognises its liability on a site-by-site basis when it can be reliably estimated. This liability includes the Group's portion of the total costs and also a portion of other potentially responsible parties' costs when it is probable that they will not be able to satisfy their respective shares of the clean-up obligation. Recoveries of reimbursements are recorded as assets when virtually certain.

Legal and other disputes

Provision is made for anticipated settlement costs where a reasonable estimate can be made of the likely outcome of legal or other disputes against the Group. In addition, provision is made for legal or other expenses arising from claims received or other disputes. In respect of product liability claims related to products where there is sufficient history of claims made and settlements, an "incurred but not reported" (IBNR) actuarial technique is used to determine a reasonable estimate of the Group's exposure to unasserted claims for those products and a provision is made on that basis.

No provision is made for other unasserted claims or where an obligation exists under a dispute but it is not possible to make a reasonable estimate. Costs associated with claims made by the Group against third parties are charged to the income statement as they are incurred.

Pensions and other post-employment benefits

The costs of providing pensions under defined benefit schemes are calculated using the projected unit credit method and spread over the period during which benefit is expected to be derived from the employees' services, in accordance with the advice of qualified actuaries. Pension obligations are measured as the present value of estimated future cash flows discounted at rates reflecting the yields of high quality corporate bonds.

Pension scheme assets are measured at fair value at the balance sheet date. Actuarial gains and losses, differences between the expected and actual returns, and the effect of changes in actuarial assumptions are recognised in the statement of recognised income and expense in the year in which they arise. The Group's contributions to defined contribution plans are charged to the income statement as incurred.

The costs of other post-employment liabilities are calculated in a similar way to defined benefit pension schemes and spread over the period during which benefit is expected to be derived from the employees' services, in accordance with the advice of qualified actuaries.

Notes to the financial statements

continued

2 Accounting policies continued

Employee share plans

Incentives in the form of shares are provided to employees under share option and share award schemes. These options and awards are fair valued at their grant dates and the cost is charged to the income statement over the relevant vesting periods. This has been applied on a fully retrospective basis. The Group provides finance to ESOP Trusts to purchase company shares on the open market to meet the obligation to provide shares when employees exercise their options or awards. Costs of running the ESOP Trusts are charged to the income statement. Shares held by the ESOP Trusts are deducted from other reserves. A transfer is made between other reserves and retained earnings over the vesting periods of the related share options or awards to reflect the ultimate proceeds receivable from employees on exercise. If there is deemed to be a permanent impairment in value this is also reflected by a transfer to retained earnings.

Property, plant and equipment

Property, plant and equipment (PP&E) is stated at the cost of purchase or construction less provisions for depreciation and impairment. Financing costs are not capitalised.

Depreciation is calculated to write off the cost less residual value of PP&E, excluding freehold land, using the straight-line basis over the expected useful life. Residual values and lives are reviewed and, where appropriate, adjusted annually. The normal expected useful lives of the major categories of PP&E are:

Freehold buildings	20 to 50 years
Leasehold land and buildings	Lease term or 20 to 50 years
Plant and machinery	10 to 20 years
Fixtures and equipment	3 to 10 years

On disposal of PP&E, the cost and related accumulated depreciation and impairments are removed from the financial statements and the net amount, less any proceeds, is taken to the income statement.

Leases

Leasing agreements which transfer to the Group substantially all the benefits and risks of ownership of an asset are treated as finance leases, as if the asset had been purchased outright. The assets are included in PP&E or computer software and the capital elements of the leasing commitments are shown as obligations under finance leases. Assets held under finance leases are depreciated on a basis consistent with similar owned assets or the lease term if shorter. The interest element of the lease rental is included in the income statement. All other leases are operating leases and the annual rentals are included in the income statement on a straight-line basis over the lease term.

Goodwill

Goodwill is stated at cost less impairments. Goodwill is deemed to have an indefinite useful life and is tested for impairment annually.

Where the fair value of the interest acquired in an entity's assets, liabilities and contingent liabilities exceeds the consideration paid, this excess is recognised immediately as a gain in the income statement.

Other intangible assets

Intangible assets are stated at cost less provisions for amortisation and impairments.

Licences, patents, know-how and marketing rights separately acquired or acquired as part of a business combination are amortised over their estimated useful lives, using the straight-line basis, from the time they are available for use. The estimated useful lives for determining the amortisation charge are reviewed annually, and take into account the estimated time it takes to bring the compounds or products to market. Any development costs incurred by the Group and associated with acquired licences, patents, know-how or marketing rights are written off to the income statement when incurred, unless the criteria for recognition of an internally generated intangible asset are met, usually when a regulatory filing has been made in a major market and approval is considered highly probable.

Brands are valued independently as part of the fair value of businesses acquired from third parties where the brand has a value which is substantial and long-term and where the brands can be sold separately from the rest of the businesses acquired. Brands are amortised over their estimated useful lives, except where it is considered that the useful economic life is indefinite.

The costs of acquiring and developing computer software for internal use and internet sites for external use are capitalised as intangible fixed assets where the software or site supports a significant business system and the expenditure leads to the creation of a durable asset. ERP systems software is amortised over seven years and other computer software over three to five years.

Impairment of non-current assets

The carrying values of all non-current assets are reviewed for impairment when there is an indication that the assets might be impaired. Additionally, goodwill, intangible assets with indefinite useful lives and intangible assets which are not yet available for use are tested for impairment annually. Any provision for impairment is charged to the income statement in the year concerned.

Investments in associates and joint ventures

Investments in associates and joint ventures are carried in the consolidated balance sheet at the Group's share of their net assets at date of acquisition and of their post-acquisition retained profits or losses together with any goodwill arising on the acquisition.

2 Accounting policies continued

Available-for-sale investments

Liquid investments and other investments are treated as available-for-sale investments and are initially recorded at cost and then remeasured at subsequent reporting dates to fair value. Unrealised gains and losses on available-for-sale investments are recognised directly in equity. On disposal or impairment of the investments, the gains and losses in equity are recycled into the income statement. Equity investments are recorded in non-current assets unless they are expected to be sold within one year.

Purchases and sales of equity investments are accounted for on the trade date and purchases and sales of other available-for-sale investments are accounted for on settlement date.

In 2004 equity investments are recorded at cost.

Inventories

Inventories are included in the financial statements at the lower of cost (including raw materials, direct labour, other direct costs and related production overheads) and net realisable value. Cost is generally determined on a first in, first out basis. Pre-launch inventory is held as an asset when there is a high probability of regulatory approval for the product. Before that point a provision is made against the carrying value to its recoverable amount, which is then reversed at the point when a high probability of regulatory approval is determined.

Trade receivables

Trade receivables are carried at original invoice amount less any provisions for doubtful debts. Provisions are made where there is evidence of a risk of non-payment, taking into account ageing, previous experience and general economic conditions. Receivables are discounted where the effect is material.

Cash and cash equivalents

Cash and cash equivalents comprise cash in hand, current balances with banks and similar institutions and highly liquid investments with maturities of three months or less when acquired. They are readily convertible into known amounts of cash and have an insignificant risk of changes in value.

Taxation

Current tax is provided at the amounts expected to be paid applying tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the temporary differences can be utilised.

Deferred tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax is provided using rates of tax that have been enacted or substantively enacted by the balance sheet date. Deferred tax liabilities and assets are not discounted.

Discounting

Where the time effect of money is material, balances are discounted to current values using appropriate rates of interest. The unwinding of the discounts is recorded in finance income/costs.

Derivative financial instruments and hedging (2006 and 2005)

Derivative financial instruments are used to manage exposure to market risks from treasury operations. The principal derivative instruments used by GlaxoSmithKline are foreign currency swaps, interest rate swaps and forward foreign exchange contracts. The Group does not hold or issue derivative financial instruments for trading or speculative purposes.

Derivative financial instruments are initially recognised in the balance sheet at cost and then remeasured at subsequent reporting dates to fair value. Derivatives designated as hedging instruments are classified on inception as fair value hedges, cash flow hedges or net investment hedges. Changes in the fair value of derivatives designated as fair value hedges are recorded in the income statement, with the changes in the fair value of the hedged asset or liability.

Changes in the fair value of derivatives designated as cash flow hedges are recognised in equity, to the extent that the hedges are effective. Ineffective portions are recognised in profit or loss immediately. Amounts deferred in equity are recycled to the income statement when the hedged item affects profit or loss.

Hedges of net investments in foreign entities are accounted for in a similar way to cash flow hedges.

Changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognised immediately in the income statement.

Derivative financial instruments and hedging (2004)

IAS 32 and 39 were adopted by the Group on 1st January 2005. In accordance with an exemption permitted under IFRS 1, the 2004 information relating to financial instruments remains as reported under UK GAAP and applying the following policies.

Derivative contracts are treated from inception as an economic hedge of the underlying financial instrument with matching accounting treatment and cash flows. Derivative instruments no longer designated as hedges are restated at market value and any future changes in value are taken directly to the profit and loss account.

Currency swaps and forward exchange contracts used to fix the value of the related asset or liability in the contract currency and at the contract rate are accrued to the profit and loss account over the life of the contract.

Gains and losses on foreign exchange contracts designated as hedges of forecast foreign exchange transactions are deferred and included in the measurement of the related foreign currency transactions in the period they occur. Gains and losses on balance sheet hedges are accrued and are taken directly to reserves except that forward premiums/discounts are recognised as interest over the life of the contracts.

Interest differentials under interest swap agreements are recognised in the profit and loss account by adjustment of interest expense over the life of the agreement.

Notes to the financial statements

continued

3 New accounting requirements

The following IFRS and IFRIC interpretations have been issued by the IASB and are likely to affect future Annual Reports, although none is expected to have a material impact on the results or financial position of the Group.

IFRS 7 'Financial instruments: disclosures' was issued in August 2005 and is required to be implemented by GSK from 1st January 2007. This new standard incorporates the disclosure requirements of IAS 32, which it supersedes, and adds further quantitative and qualitative disclosures in relation to financial instruments.

Amendment to IAS 1 'Capital disclosures' was issued in August 2005 and is required to be implemented by GSK from 1st January 2007. The amendment requires new disclosures about how an entity manages its capital resources.

IFRS 8 'Operating segments' was issued in November 2006 and is required to be implemented by GSK from 1st January 2009. This standard replaces IAS 14 and aligns the segmental reporting requirements with those of the equivalent US standard. The new standard adopts a 'management approach' under which segmental information is to be disclosed on the same basis as that used for internal reporting purposes.

IFRIC 9 'Reassessment of embedded derivatives' was issued in March 2006 and is required to be implemented by GSK from 1st January 2007. This interpretation clarifies that an embedded derivative should be assessed on its inception and only reassessed if there is a change in the terms of the relevant contract.

IFRIC 10 'Interim financial reporting and impairment' was issued in July 2006 and is required to be implemented by GSK from 1st January 2007. Under this interpretation any impairment losses on goodwill and equity investments recognised in a quarterly interim statement may not be reversed in subsequent interim or annual financial statements.

IFRIC 11 'IFRS 2 - Group and treasury share transactions' was issued in November 2006 and is required to be implemented by GSK from 1st January 2008. This interpretation provides guidance on whether share-based transactions involving group entities should be accounted for as equity settled or cash settled transactions.

4 Exchange rates

The Group uses the average of exchange rates prevailing during the period to translate the results and cash flows of overseas subsidiaries, joint ventures and associated undertakings into Sterling and period end rates to translate the net assets of those undertakings. The currencies which most influence these translations, and the relevant exchange rates, were:

	2006	2005	2004
Average rates:			
£/US\$	1.85	1.82	1.83
£/Euro	1.47	1.46	1.47
£/Yen	215	200	197
Period end rates:			
£/US\$	1.96	1.72	1.92
£/Euro	1.48	1.46	1.41
£/Yen	233	203	197

5 Segment information

The Group's primary segment reporting is by business sector with geographical reporting being the secondary format. The business sectors consist of Pharmaceuticals (prescription pharmaceuticals and vaccines) and Consumer Healthcare (oral care, OTC medicines and nutritional healthcare). The geographical sectors of the USA, Europe and International (other Rest of World markets) reflect the Group's most significant regional markets and are consistent with the Group's regional market management reporting structure. Business sector data includes an allocation of corporate costs to each sector on an appropriate basis. There are no sales between business sectors. The Group's activities are organised on a global basis. The geographical sector figures are therefore influenced by the location of the Group's operating resources, in particular manufacturing and research, and by variations over time in intra-Group trading and funding arrangements. Turnover is shown by business sector, by location of customer and by location of subsidiary. Other geographic information is given by location of subsidiary. The UK segment information gives turnover by location of customer and location of subsidiary. The UK operating profit, total assets and net assets are also shown. Where the Group co-promotes a product and the third party records the sale, the Group records its share of revenue as co-promotion income within turnover. The nature of co-promotion activities is such that the Group records no costs of sales. Pharmaceutical turnover includes co-promotion revenue of £182 million (2005 – £112 million, 2004 – £65 million).

5 Segment information continued

	2006 £m	2005 £m	2004 £m
Turnover by business sector			
Pharmaceuticals	20,078	18,661	17,100
Consumer Healthcare	3,147	2,999	2,886
Turnover	23,225	21,660	19,986
Profit by business sector			
Pharmaceuticals	7,125	6,159	5,126
Consumer Healthcare	683	715	630
Operating profit	7,808	6,874	5,756
Finance income	287	257	176
Finance costs	(352)	(451)	(362)
Share of after tax profits of associates and joint ventures:			
Pharmaceuticals	56	52	60
Consumer Healthcare	–	–	–
Profit on disposal of interest in associates	–	–	149
Profit before taxation	7,799	6,732	5,779
Taxation	(2,301)	(1,916)	(1,757)
Profit after taxation for the year	5,498	4,816	4,022
Investments in associates and joint ventures by business sector			
Pharmaceuticals	295	276	
Consumer Healthcare	–	–	
Investment in associates and joint ventures	295	276	
Property, plant and equipment and other intangible assets by business sector			
Additions			
Pharmaceuticals	1,795	2,031	
Consumer Healthcare	139	164	
Total additions	1,934	2,195	
Depreciation/amortisation			
Pharmaceuticals	(849)	(807)	
Consumer Healthcare	(109)	(97)	
Total depreciation/amortisation	(958)	(904)	
Impairment			
Pharmaceuticals	(241)	(92)	
Consumer Healthcare	(3)	–	
Total impairment	(244)	(92)	
Impairment reversal			
Pharmaceuticals	61	3	
Consumer Healthcare	–	–	
Total impairment reversal	61	3	

Notes to the financial statements

continued

5 Segment information continued

	2006 £m	2005 £m	
Total assets by business sector			
Pharmaceuticals	16,936	16,431	
Consumer Healthcare	2,768	2,446	
Total operating assets	19,704	18,877	
Investments in associates and joint ventures	295	276	
Liquid investments	1,035	1,025	
Derivative financial instruments	193	179	
Cash and cash equivalents	2,005	4,209	
Current and deferred taxation	2,309	2,630	
Tangible assets held for sale	12	2	
Total assets	25,553	27,198	
Total liabilities by business sector			
Pharmaceuticals	(8,148)	(9,099)	
Consumer healthcare	(951)	(1,070)	
Total operating liabilities	(9,099)	(10,169)	
Short-term borrowings	(718)	(1,200)	
Long-term borrowings	(4,772)	(5,271)	
Derivative financial instruments	(100)	(150)	
Current and deferred taxation	(1,216)	(2,838)	
Total liabilities	(15,905)	(19,628)	
Net assets by business sector			
Pharmaceuticals	8,788	7,332	
Consumer Healthcare	1,817	1,376	
Net operating assets	10,605	8,708	
Net debt	(2,450)	(1,237)	
Investments in associates and joint ventures	295	276	
Derivative financial instruments	93	29	
Current and deferred taxation	1,093	(208)	
Tangible assets held for sale	12	2	
Net assets	9,648	7,570	
Turnover by location of customer			
	2006 £m	2005 £m	2004 £m
USA	11,102	9,867	9,191
Europe	7,010	6,892	6,395
International	5,113	4,901	4,400
Turnover	23,225	21,660	19,986
Turnover by location of subsidiary undertaking			
USA	11,362	10,185	9,511
Europe	14,007	12,303	11,192
International	9,349	8,547	7,787
Turnover including inter-segment turnover	34,718	31,035	28,490
USA	339	308	327
Europe	6,337	4,836	4,304
International	4,817	4,231	3,873
Inter-segment turnover	11,493	9,375	8,504
USA	11,023	9,877	9,184
Europe	7,670	7,467	6,888
International	4,532	4,316	3,914
External turnover	23,225	21,660	19,986

5 Segment information continued

Property, plant and equipment and other intangible asset additions by location	2006 £m	2005 £m
USA	637	509
Europe	1,020	742
International	277	944
Total additions	1,934	2,195

Total assets by location

USA	4,830	4,459
Europe	15,166	16,423
International	5,389	5,020
Inter-segment trading balances	(5,681)	(7,025)
Total operating assets	19,704	18,877
Investments in associates and joint ventures	295	276
Liquid investments	1,035	1,025
Derivative financial instruments	193	179
Cash and cash equivalents	2,005	4,209
Current and deferred taxation	2,309	2,630
Tangible assets held for sale	12	2
Total assets	25,553	27,198

Net assets by location

USA	919	446
Europe	11,151	11,628
International	4,216	3,659
Inter-segment trading balances	(5,681)	(7,025)
Net operating assets	10,605	8,708
Net debt	(2,450)	(1,237)
Investments in associates and joint ventures	295	276
Derivative financial instruments	93	29
Current and deferred taxation	1,093	(208)
Tangible assets held for sale	12	2
Net assets	9,648	7,570

UK segment

For the purposes of US GAAP information is given separately in respect of the UK, which, although included in the Group's Europe market region, is considered the Group's home segment for the purposes of segmental reporting.

	2006 £m	2005 £m	2004 £m
Turnover by location of customer	1,501	1,431	1,382
Turnover including inter-segment turnover	4,890	4,414	4,386
Inter-segment turnover	3,086	2,657	2,709
Turnover by location of subsidiary	1,804	1,757	1,677
Operating profit	1,468	1,576	1,327
Total assets	6,208	7,057	6,521
Net operating assets	2,829	2,290	2,253

Notes to the financial statements

continued

6 Other operating income

	2006 £m	2005 £m	2004 £m
Royalties	112	83	96
Asset disposal profits	169	290	146
Other income including fair value adjustments	26	(9)	(7)
	307	364	235

Royalties are principally a core of recurring income from the out-licensing of intellectual property. Asset disposal profits include product divestments and disposals of equity investments, intellectual property and tangible property. Other income includes equity investment carrying value adjustments arising from stock market changes and fair value adjustments arising on the Quest Collar and Theravance put and call options.

7 Operating profit

	2006 £m	2005 £m	2004 £m
The following items have been charged in operating profit:			
Employee costs (Note 8)	5,495	5,254	5,054
Advertising	759	697	599
Distribution costs	276	270	266
Depreciation of property, plant and equipment	732	710	691
Amortisation of intangible assets	226	194	168
Net foreign exchange losses/(gains)	36	(3)	72
Inventories:			
Cost of inventories included in cost of sales	4,480	4,335	4,032
Write-down of inventories	146	119	142
Reversal of prior year write-down of inventories	(93)	(61)	(49)
Operating lease rentals:			
Minimum lease payments	114	104	110
Contingent rents	11	12	9
Sub-lease payments	2	1	–
Fees payable to company's auditor for the audit of parent company and consolidated financial statements	1.7	1.4	1.1
Fees payable to the company's auditor and its associates for other services	15.9	13.1	13.4

The reversals of prior year write-downs of inventories principally arise from the reassessment of usage or demand expectations prior to inventory expiration.

	2006 £m	2005 £m	2004 £m
Fees payable to the company's auditor and its associates for other services			
Audit of accounts of the Group's UK and overseas subsidiaries and related pension schemes of the company, pursuant to legislation	7.7	6.7	5.7
Other assurance services, pursuant to such legislation	4.4	2.6	2.2
Other tax services	1.9	2.3	3.0
All other services, including regulatory, compliance and treasury related services	1.9	1.5	2.5
	15.9	13.1	13.4

At 31st December 2006, the amount due to PricewaterhouseCoopers LLP and its associates for fees yet to be invoiced was £3.7 million, comprising statutory audit £3.4 million and taxation services £0.3 million.

Fees in respect of the GlaxoSmithKline plc pension scheme included above:

	2006 £m	2005 £m	2004 £m
Audit	0.3	0.2	0.2
Other services	0.1	–	–
	0.4	0.2	0.2

8 Employee costs

	2006 £m	2005 £m	2004 £m
Wages and salaries	4,363	4,152	3,864
Social security costs	461	432	430
Pension and other post-employment costs (Note 26)	377	350	347
Cost of share-based incentive plans	226	236	333
Severance and other costs from integration and restructuring activities	68	84	80
	5,495	5,254	5,054

The Group provides benefits to employees, commensurate with local practice in individual countries, including, in some markets, healthcare insurance, subsidised car schemes and personal life assurance.

The average number of persons employed by the Group (including Directors) during the year	2006 Number	2005 Number	2004 Number
Manufacturing	32,403	30,906	31,427
Selling, general and administration	53,665	53,634	53,513
Research and development	15,734	14,963	14,897
	101,802	99,503	99,837

The average number of Group employees excludes temporary and contract staff. The numbers of Group employees at the end of each financial year are given in the Financial record on page 181. The average number of persons employed by GlaxoSmithKline plc in 2006 was nil (2005 – nil).

The compensation of the Directors and Senior Management (members of the CET and the Company Secretary) in aggregate, was as follows:

	2006 £m	2005 £m	2004 £m
Wages and salaries	15	17	13
Social security costs	1	1	1
Pension and other post-employment costs	3	3	2
Cost of share-based incentive plans	14	15	16
	33	36	32

9 Finance income

	2006 £m	2005 £m	2004 £m
Interest income	262	268	173
Unwinding of discount on assets	1	–	3
Interest on extended credit on receivables	21	8	–
Net investment hedges	(2)	(17)	–
Fair value adjustments on non-hedging derivatives	4	(2)	–
Realised gains on financial instruments	1	–	–
	287	257	176

10 Finance costs

	2006 £m	2005 £m	2004 £m
Interest on bank loans and overdrafts	(5)	(11)	(6)
Interest on other loans	(301)	(412)	(337)
Interest in respect of finance leases	(8)	(4)	(2)
Realised losses on financial instruments	–	–	(1)
Unwinding of discount on provisions	(36)	(25)	(16)
Fair value hedges	–	2	–
Fair value adjustments on non-hedging derivatives	(2)	(1)	–
	(352)	(451)	(362)

Notes to the financial statements

continued

11 Associates and joint ventures

	2006 £m	2005 £m	2004 £m
Associates:			
Share of after tax profits of Quest Diagnostics Inc.	59	52	59
Share of after tax losses of other associates	(2)	(1)	(1)
	57	51	58
Share of after tax (losses)/profits of joint ventures	(1)	1	2
	56	52	60
Share of turnover of joint ventures	21	32	31
Sales to joint ventures and associates	18	48	50

Summarised income statement information in respect of the Group's associates is set out below:

	2006 £m	2005 £m	2004 £m
Total turnover	3,392	3,029	2,806
Total profit	315	296	275

12 Taxation

Taxation charge based on profits for the year

	2006 £m	2005 £m	2004 £m
UK corporation tax at the UK statutory rate	2,512	407	304
Less double taxation relief	(2,112)	(235)	(156)
	400	172	148
Overseas taxation	2,310	1,847	1,519
Current taxation	2,710	2,019	1,667
Deferred taxation	(409)	(103)	90
	2,301	1,916	1,757

Reconciliation of the taxation rate on Group profits

	2006 %	2005 %	2004 %
UK statutory rate of taxation	30.0	30.0	30.0
Overseas taxes	4.2	3.0	2.5
Benefit of special tax status	(5.2)	(2.3)	(3.6)
R&D credits	(1.3)	(1.4)	(1.5)
Intercompany stock profit	(1.9)	1.0	0.3
Impact of share based payments	0.5	(0.3)	1.5
Tax on profit of associates	(0.4)	(0.4)	(0.4)
Other differences	0.3	(0.4)	0.5
Prior year items	3.3	(0.7)	1.1
Tax rate	29.5	28.5	30.4

Additional UK Corporation tax and Double Taxation relief in 2006 arise from dividends received from overseas subsidiaries. Current tax expense has been reduced by a benefit of £5 million arising from previously unrecognised tax losses. Deferred tax expense has been reduced by a benefit of £2 million arising from changes in tax rates.

The Group operates in countries where the tax rate differs from the UK tax rate. The impact of these overseas taxes on the company's overall rate of tax is shown above. Profits arising from certain operations in Singapore, Puerto Rico, Ireland and Belgium are accorded special status and are taxed at reduced rates compared with the normal rates of tax in these territories. The effect of this reduction in the taxation charge increased earnings per share by 7.2p in 2006, 2.7p in 2005 and 3.6p in 2004.

The Group is required under IFRS to create a deferred tax asset in respect of unrealised intercompany profit arising on stock held by the Group at the year end by applying the tax rate of the country in which the stock is held (rather than the tax rate of the country where the profit was originally made and the tax paid, which is the practice under UK and US GAAP). The Group tax rate was decreased by 1.9% in 2006 (2005 – 1.0% increase, 2004 – 0.3% increase) as a result of increases in work-in-progress and finished goods.

The integrated nature of the Group's worldwide operations, involving significant investment in research and strategic manufacture at a limited number of locations, with consequential cross-border supply routes into numerous end-markets, gives rise to complexity and delay in negotiations with revenue authorities as to the profits on which individual Group companies are liable to tax. Resolution of such issues is a continuing fact of life for GSK.

12 Taxation continued

As reported last year, GSK's largest unresolved tax issues were with the US Internal Revenue Service (IRS) and UK HM Revenue and Customs (HMRC) in respect of transfer prices related to the Glaxo heritage products.

On 11th September 2006, GSK and the IRS agreed to a resolution of their dispute. Under the agreement, GSK has made gross payments to the IRS of approximately \$3.3 billion. The final net cash cost to the Group is approximately \$3.1 billion, which covers federal, state and local taxes, interest and the benefit of tax relief on the payments made. The settlement resolved all the transfer pricing issues in dispute for the period 1989 – 2000, which were due to go to trial in February 2007, and also covers the subsequent years 2001 – 2005. GSK had previously made provision for the dispute and this settlement did not have any significant impact on the Group's reported earnings or tax rate for the year.

GSK continues to be in dispute with HMRC primarily in respect of transfer pricing and Controlled Foreign Companies legislation matters for the years 1994 to date and the parties are now preparing for litigation. HMRC has not formally quantified its claims in respect of these matters but there continues to be a wide difference between the Group and HMRC positions on these matters. GSK also has open issues in Japan and Canada, which were the subject of court proceedings in 2006. In Japan the tax authorities are claiming approximately Yen 39 billion (£169 million) in respect of transactions in 1998. GSK has paid the tax claimed, as required by law, and applied for a refund. A court decision is expected in late March 2007. A court decision in the Group's dispute with the Canadian Revenue Authority over the pricing of *Zantac* in the years 1989 to 1993 is expected in the first half of 2007.

GSK uses the best advice in determining its transfer pricing methodology and in seeking to manage transfer pricing and other taxation issues to a satisfactory conclusion and, on the basis of external professional advice, continues to believe that it has made adequate provision for the liabilities likely to arise from open assessments. The ultimate liability for such matters may vary from the amounts provided and is dependent upon the outcome of litigation proceedings and negotiations with the relevant tax authorities.

Except as shown in this Annual Report, no provision has been made for taxation which would arise on the distribution of profits retained by overseas subsidiary and associated undertakings, on the grounds that no remittance of profit retained at 31st December 2006 is required in such a way that incremental tax will arise. The aggregate amount of these unremitted profits at the balance sheet date was approximately £26 billion.

Movement on current tax account	Payable £m	Recoverable £m	Net £m
At 1st January 2006	(2,269)	416	(1,853)
Exchange adjustments	170	(8)	162
Charge for the year	(1,981)	(729)	(2,710)
Cash paid	3,438	408	3,846
Other movements	21	99	120
At 31st December 2006	(621)	186	(435)

Movement in deferred tax assets and liabilities

Deferred taxation asset/(liability)	Accelerated capital allowances	Intangibles	Intra-group profit	Product & business disposals	Pensions & other post retirement benefits	Tax Losses	Legal & other disputes	Manu- facturing restructuring	Stock valuation adjustments	Share option and award schemes	Other net temporary differences	Total
Deferred tax asset at 1st January 2006	(492)	(18)	709	(9)	1,035	63	160	73	(72)	151	614	2,214
Deferred tax liability at 1st January 2006	(123)	(522)	–	13	25	24	1	–	(50)	–	63	(569)
At 1st January 2006	(615)	(540)	709	4	1,060	87	161	73	(122)	151	677	1,645
Exchange adjustments	11	27	–	–	(55)	(10)	(17)	(1)	8	–	(82)	(119)
Credit/(charge) to income	(5)	113	225	(9)	33	15	9	7	16	5	–	409
Credit/(charge) to equity	–	–	–	–	(161)	–	–	–	–	1	(13)	(173)
Transfer to/from current tax	2	–	–	4	(139)	–	–	(5)	3	–	(20)	(155)
Acquisitions	–	(84)	–	–	–	1	–	–	–	–	4	(79)
Other movements	–	–	–	–	–	5	–	–	5	–	(10)	–
At 31st December 2006	(607)	(484)	934	(1)	738	98	153	74	(90)	157	556	1,528
Deferred tax asset at 31st December 2006	(34)	(49)	934	–	416	64	147	30	(35)	124	526	2,123
Deferred tax liability at 31st December 2006	(573)	(435)	–	(1)	322	34	6	44	(55)	33	30	(595)
	(607)	(484)	934	(1)	738	98	153	74	(90)	157	556	1,528

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12 Taxation continued

At 31st December 2006, the Group had recognised a deferred tax asset of £98 million (2005 – £87 million) in respect of income tax losses of approximately £348 million (2005 – £291 million). Of these losses, £100 million (2005 – £64 million) are due to expire between 2007–2013, £178 million (2005 – £184 million) are due to expire between 2019–2027 and £70 million (2005 – £43 million) are available indefinitely. At 31st December 2006, the Group had not recognised any deferred tax asset in respect of income tax losses of approximately £3,742 million (2005 – £217 million), of which £131 million (2005 – £28 million) are due to expire between 2007–2018, £21 million (2005 – £79 million) are due to expire between 2019–2027 and £3,590 million (2005 – £110 million) are available indefinitely. Unrecognised losses have increased in 2006 due to quantification of previously uncertain amounts arising principally in 2003 and 2004. The Group had capital losses at 31st December 2006 estimated to be in excess of £10 billion in respect of which no deferred tax asset has been recognised. Deferred tax assets are recognised where it is probable that future taxable profit will be available to utilise losses. All deferred taxation movements arise from the origination and reversal of temporary differences. Other net temporary differences include accrued expenses and other provisions.

13 Earnings per share

	2006 p	2005 p	2004 p
Basic earnings per share	95.5	82.6	68.1
Diluted earnings per share	94.5	82.0	68.0

Basic earnings per share have been calculated by dividing the profit attributable to shareholders by the weighted average number of shares in issue during the period after deducting shares held by the ESOP Trusts and treasury shares.

Diluted earnings per share have been calculated after adjusting the weighted average number of shares used in the basic calculation to assume the conversion of all potentially dilutive shares. A potentially dilutive share forms part of the employee share schemes where its exercise price is below the average market price of GSK shares during the period and any performance conditions attaching to the scheme have been met at the balance sheet date.

The number of shares used in calculating basic and diluted earnings per share are reconciled below.

Weighted average number of shares in issue	millions	millions	millions
Basic	5,643	5,674	5,736
Dilution for share options	57	46	12
Diluted	5,700	5,720	5,748

Shares held by the ESOP Trusts are excluded. The trustees have waived their rights to dividends on the shares held by the ESOP Trusts.

14 Dividends

2006	First interim	Second interim	Third interim	Fourth interim	Total
Total dividend (£m)	619	620	671	785	2,695
Dividend per share (pence)	11	11	12	14	48
Paid/payable	6th July 2006	5th October 2006	4th January 2007	12th April 2007	

2005					
Total dividend (£m)	568	567	568	791	2,494
Dividend per share (pence)	10	10	10	14	44
Paid	7th July 2005	6th October 2005	5th January 2006	6th April 2006	

2004					
Total dividend (£m)	575	573	571	684	2,403
Dividend per share (pence)	10	10	10	12	42
Paid	1st July 2004	30th September 2004	6th January 2005	7th April 2005	

Under IFRS interim dividends are only recognised in the financial statements when paid and not when declared. GSK normally pays a dividend two quarters after the quarter to which it relates and one quarter after it is declared. The 2006 financial statements recognise those dividends paid in 2006, namely the third and fourth interim dividends for 2005 and the first and second interim dividends for 2006. The amounts recognised in each year are as follows:

	2006 £m	2005 £m	2004 £m
Dividends to shareholders	2,598	2,390	2,476

15 Property, plant and equipment

	Land and buildings £m	Plant, equipment and vehicles £m	Assets in construction £m	Total £m
Cost at 1st January 2005	4,062	7,512	682	12,256
Exchange adjustments	136	183	19	338
Additions	54	307	640	1,001
Additions through business combinations	32	45	33	110
Disposals and write-offs	(82)	(404)	(4)	(490)
Reclassifications	83	255	(348)	(10)
Transfer to assets held for sale	(4)	(11)	–	(15)
Cost at 31st December 2005	4,281	7,887	1,022	13,190
Exchange adjustments	(232)	(295)	(65)	(592)
Additions	100	403	982	1,485
Additions through business combinations	–	5	–	5
Disposals and write-offs	(44)	(578)	(5)	(627)
Reclassifications	153	358	(511)	–
Transfer to assets held for sale	(14)	(4)	–	(18)
Cost at 31st December 2006	4,244	7,776	1,423	13,443
Depreciation at 1st January 2005	(1,171)	(4,578)	–	(5,749)
Exchange adjustments	(38)	(119)	–	(157)
Provision for the year	(125)	(585)	–	(710)
Disposals and write-offs	43	356	–	399
Reclassifications	–	1	–	1
Transfer to assets held for sale	1	10	–	11
Depreciation at 31st December 2005	(1,290)	(4,915)	–	(6,205)
Exchange adjustments	73	196	–	269
Provision for the year	(137)	(595)	–	(732)
Disposals and write-offs	23	506	–	529
Transfer to assets held for sale	6	3	–	9
Depreciation at 31st December 2006	(1,325)	(4,805)	–	(6,130)
Impairment at 1st January 2005	(136)	(147)	(27)	(310)
Exchange adjustments	(9)	(2)	–	(11)
Disposals and write-offs	10	2	2	14
Impairment losses	(13)	(18)	–	(31)
Reversal of impairments	–	3	–	3
Transfer to assets held for sale	2	–	–	2
Impairment at 31st December 2005	(146)	(162)	(25)	(333)
Exchange adjustments	13	4	3	20
Disposals and write-offs	12	10	2	24
Impairment losses	(46)	(107)	(2)	(155)
Reversal of impairments	26	24	11	61
Impairment at 31st December 2006	(141)	(231)	(11)	(383)
Total depreciation and impairment at 31st December 2005	(1,436)	(5,077)	(25)	(6,538)
Total depreciation and impairment at 31st December 2006	(1,466)	(5,036)	(11)	(6,513)
Net book value at 1st January 2005	2,755	2,787	655	6,197
Net book value at 31st December 2005	2,845	2,810	997	6,652
Net book value at 31st December 2006	2,778	2,740	1,412	6,930

The net book value at 31st December 2006 of the Group's land and buildings comprises freehold properties £2,632 million (2005 – £2,635 million), properties with leases of 50 years or more £116 million (2005 – £155 million) and properties with leases of less than 50 years £30 million (2005 – £55 million).

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15 Property, plant and equipment continued

Included in land and buildings at 31st December 2006 are leased assets with a cost of £241 million (2005 – £165 million), accumulated amortisation of £95 million (2005 – £49 million) and a net book value of £146 million (2005 – £116 million). Included in plant, equipment and vehicles at 31st December 2006 are leased assets with a cost of £263 million (2005 – £153 million), accumulated amortisation of £97 million (2005 – £57 million) and a net book value of £166 million (at 1st January 2006 – £96 million). Some lease agreements include renewal or purchase options or escalation clauses.

The impairment losses principally arise from decisions to rationalise facilities and are calculated based on either fair value less costs to sell or value in use. The value in use calculations determine the net present value of the projected risk-adjusted, post-tax cash flows of the relevant asset or cash generating unit, applying a discount rate of the Group post-tax weighted average cost of capital of 8%, adjusted where appropriate for country specific risks. These losses have been charged through cost of sales £125 million, R&D £22 million, and SG&A £8 million.

Reversals of impairment arise from subsequent reviews of the impaired assets where the conditions which gave rise to the original impairments are deemed no longer to apply. The principal component of the 2006 reversals relates to the Montrose manufacturing facility, and all of the reversals have been credited to cost of sales.

16 Goodwill

	2006 £m	2005 £m
Cost at 1st January	696	304
Exchange adjustments	(54)	10
Additions through business combinations	126	383
Disposals	–	(1)
Impairments	(10)	–
Cost at 31st December	758	696
Net book value at 1st January	696	304
Net book value at 31st December	758	696

The additions for the year comprise £112 million on the acquisition of CNS, Inc., £8 million on the acquisition of Pliva Research Institute and a further £6 million on the acquisition of the minority interest held in GlaxoSmithKline K.K. See Note 36 for further details.

The impairments in the year of £10 million relate to the Europharm business located in Romania and were determined using the fair value less costs to sell model.

The carrying value of goodwill is made up of balances arising on acquisition of the following companies:

	2006 £m	2005 £m
ID Biomedical Corporation	316	358
CNS, Inc.	112	–
Nippon Glaxo	134	143
Polfa Poznan S.A.	96	98
Corixa Corporation	25	28
Others	75	69
	758	696

Goodwill is allocated to cash generating units which are tested for impairment at least annually. The recoverable amounts of the cash generating units are assessed using a value in use or a fair value less costs to sell model, depending on the nature of the unit. Value in use is calculated as the net present value of the projected risk-adjusted, five-year post-tax cash flows plus a terminal value of the cash generating unit to which the goodwill is allocated. Initially a post-tax discount rate based on the Group's weighted average cost of capital of 8%, adjusted where appropriate for country specific risks, is applied to calculate the net present value of the post-tax cash flows. Where this indicates that the recoverable value of the unit is close to or below its carrying value, the impairment test is reperformed using a pre-tax discount rate and pre-tax cash flows in order to determine if an impairment exists and to establish its magnitude. Fair value is calculated using a discounted cash flow approach, which in this case is based on the Group's acquisition valuation model.

The cash generating units for which the carrying amount of goodwill allocated to the unit is significant in comparison with the total goodwill balance are Vaccines, Consumer Healthcare, Japan and Poland. Total goodwill of £362 million (2005 – £407 million), principally relating to the acquisitions of ID Biomedical and Corixa, is allocated to the Vaccines unit. The recoverable value of this unit is determined using the fair value less costs to sell model. Goodwill arising on the acquisition of the minority interest in Nippon Glaxo of £134 million (2005 – £143 million) and on the acquisition of Polfa Poznan of £96 million (2005 – £98 million) is allocated to the Japan and Poland cash generating units respectively. The recoverable value of both these units is determined using the value in use model. Goodwill arising on the acquisition of CNS, Inc. in December 2006 is allocated to the Consumer Healthcare cash generating unit.

17 Other intangible assets

	Computer software £m	Licences, patents, etc. £m	Brands £m	Total £m
Cost at 1st January 2005	609	1,449	1,143	3,201
Exchange adjustments	13	72	41	126
Additions	62	207	–	269
Additions through business combinations	–	816	–	816
Disposals and asset write-offs	(9)	(72)	–	(81)
Reclassifications from property, plant and equipment	10	–	–	10
Cost at 31st December 2005	685	2,472	1,184	4,341
Exchange adjustments	(23)	(213)	(62)	(298)
Additions	90	138	–	228
Additions through business combinations	–	29	187	216
Disposals and asset write-offs	(37)	(80)	–	(117)
Cost at 31st December 2006	715	2,346	1,309	4,370
Amortisation at 1st January 2005	(314)	(265)	–	(579)
Exchange adjustments	(6)	(21)	–	(27)
Provision for the year	(85)	(109)	–	(194)
Disposals and asset write-offs	7	10	–	17
Reclassifications from property, plant and equipment	(1)	–	–	(1)
Amortisation at 31st December 2005	(399)	(385)	–	(784)
Exchange adjustments	13	38	–	51
Provision for the year	(87)	(139)	–	(226)
Disposals and asset write-offs	29	7	–	36
Amortisation at 31st December 2006	(444)	(479)	–	(923)
Impairment at 1st January 2005	(23)	(65)	(21)	(109)
Exchange adjustments	–	(2)	(2)	(4)
Impairment losses	(1)	(60)	(1)	(62)
Disposals and asset write-offs	1	–	–	1
Impairment at 31st December 2005	(23)	(127)	(24)	(174)
Exchange adjustments	–	29	3	32
Impairment losses	(9)	(80)	–	(89)
Disposals and asset write-offs	8	69	–	77
Impairment at 31st December 2006	(24)	(109)	(21)	(154)
Total amortisation and impairment at 31st December 2005	(422)	(512)	(24)	(958)
Total amortisation and impairment at 31st December 2006	(468)	(588)	(21)	(1,077)
Net book value at 1st January 2005	272	1,119	1,122	2,513
Net book value at 31st December 2005	263	1,960	1,160	3,383
Net book value at 31st December 2006	247	1,758	1,288	3,293

Notes to the financial statements

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17 Other intangible assets continued

Amortisation and impairment have been charged through R&D, and SG&A. At 31st December 2006, the net book value of computer software included £28 million that had been internally generated.

The additions through business combinations in the year of £216 million include £207 million from CNS, Inc. (Note 36).

Brands comprise a portfolio of products acquired with the acquisitions of Sterling Winthrop Inc. in 1994, The Block Drug Company in 2001 and CNS, Inc. in 2006. The book values of the major brands are as follows:

	2006 £m	2005 £m
<i>Panadol</i>	317	340
<i>Sensodyne</i>	220	230
<i>Breathe Right</i>	169	–
<i>Polident</i>	93	97
<i>Corega</i>	83	87
<i>Poligrip</i>	57	60
<i>Solpadeine</i>	56	56
Others	293	290
	1,288	1,160

Each of these brands is considered to have an indefinite life, given the strength and durability of the brand and the level of marketing support. The brands are in relatively similar stable and profitable market sectors, with similar risk profiles, and their size, diversification and market shares mean that the risk of market-related factors causing a shortening of the brands' lives is considered to be relatively low. The Group is not aware of any material legal, regulatory, contractual, competitive, economic or other factor which could limit their useful lives. Accordingly, they are not amortised. Each brand is tested annually for impairment applying a fair value less costs to sell methodology and using five year post-tax cash flow forecasts with a terminal value calculation and applying a discount rate of the Group post-tax weighted average cost of capital of 8%, adjusted where appropriate for country-specific risks.

The main assumptions include future sales prices and volumes, product contribution, the future expenditure required to maintain the product's marketability and registration in the relevant jurisdiction and the product's life. These assumptions are reviewed as part of management's budgeting and strategic planning cycle for changes in market conditions and sales erosion through competition.

18 Investments in associates and joint ventures

	Joint ventures £m	Associated undertakings £m	2006 Total £m	2005 Total £m
At 1st January	14	262	276	209
Implementation of accounting for financial instruments under IAS 39	–	–	–	(7)
At 1st January, as adjusted	14	262	276	202
Exchange adjustments	(2)	(35)	(37)	26
Additions	8	5	13	2
Fair value adjustment	–	1	1	–
Retained profit for the year	(4)	46	42	46
At 31st December	16	279	295	276

The principal associated undertaking is Quest Diagnostics Inc. a US clinical laboratory business listed on the New York Stock Exchange.

The investment had a book value at 31st December 2006 of £262 million (2005 – £244 million) and a market value of £987 million (2005 – £1,093 million).

At 31st December 2006, the Group owned 18.7% of Quest (2005 – 18.4%). Although the Group holds less than 20% of the ownership interest and voting control in Quest, the Group has the ability to exercise significant influence through both its significant shareholding and its nominated director's active participation on the Quest Board of Directors and Board sub-committees.

18 Investments in associates and joint ventures continued

Summarised balance sheet information in respect of the Group's associates is set out below:

	2006 £m	2005 £m
Total assets	2,930	3,134
Total liabilities	(1,350)	(1,481)
Net assets	1,580	1,653
Group's share of associates' net assets	279	262

Investments in joint ventures comprise £22 million share of gross assets (2005 – £17 million) and £6 million share of gross liabilities (2005 – £3 million). These principally arise from 50% interests in two joint ventures, Shionogi-GlaxoSmithKline Holdings, L.P., which is developing specified chemical compounds, and GlaxoSmithKline Shire BioChem, which primarily co-markets *Combivir*, *Trizivir* and *Epivir* in certain territories, together with a 29% interest in another joint venture, Pharmaceutical Insurance Limited, which is a mutual insurance company covering pharmaceutical property risk.

In 2002, GSK hedged part of the equity value of its holding in Quest Diagnostics Inc. through a series of variable sale forward contracts. The contracts ('the equity collar') were renewed in 2006 and are structured in five series, each over two million Quest shares, and mature between 2010 and 2012. The fair value of the contracts at 31st December 2006 was a liability of \$24 million (2005 – \$24 million).

19 Other investments

	2006 £m	2005 £m
At 1st January	362	298
Implementation of accounting for financial instruments under IAS 39	–	61
At 1st January as adjusted	362	359
Exchange adjustments	(45)	33
Additions	57	23
Fair value movements	116	14
Impairments	(16)	(35)
Transfers	–	(12)
Disposals	(33)	(20)
At 31st December	441	362

Other investments comprise non-current equity investments which are available-for-sale investments recorded at fair value at each balance sheet date. For investments traded in an active market, the fair value is determined by reference to the relevant stock exchange quoted bid price. For other investments, the fair value is estimated by reference to the current market value of similar instruments or by reference to the discounted cash flows of the underlying net assets.

The Group holds a number of equity investments, frequently in entities where the Group has entered into research collaborations. Equity investments are recorded as non-current assets unless they are expected to be sold within one year, in which case they are recorded as current assets. Non-current equity investments include listed investments of £348 million (2005 – £268 million) that offer the Group the opportunity for return through dividend income and fair value gains.

On disposal of investments, fair value movements are reclassified from reserves to the income statement based on average cost.

The impairment losses recorded in the tables above have been recognised in the income statement for the year within other operating income, together with amounts recycled from the fair value reserve (Note 32) on recognition of the impairments. These impairments initially result from prolonged or significant declines in the fair value of the equity investments below acquisition cost, subsequent to which any further declines in fair value are immediately taken to the income statement.

20 Other non-current assets

	2006 £m	2005 £m
Amounts recoverable under insurance contracts	262	265
Derivative financial instruments	113	15
Pension schemes in surplus	179	12
Other receivables	167	146
	721	438

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21 Inventories

	2006 £m	2005 £m
Raw materials and consumables	764	721
Work in progress	626	552
Finished goods	1,047	904
	2,437	2,177

22 Trade and other receivables

	2006 £m	2005 £m
Trade receivables	4,356	4,411
Prepaid pension contributions	1	1
Other prepayments and accrued income	223	285
Interest receivable	28	42
Employee loans and advances	51	59
Derivative financial instruments	80	180
Other receivables	578	370
	5,317	5,348

Trade receivables include £13 million (2005 – £2 million) due from associates and joint ventures.

Movements in the bad and doubtful debt provision are as follows:

	2006 £m	2005 £m
At 1st January	140	128
Exchange adjustments	(9)	8
Charge for the year	12	40
Utilised	(39)	(36)
At 31st December	104	140

23 Cash and cash equivalents

	2006 £m	2005 £m
Cash at bank and in hand	620	686
Short-term deposits	1,324	1,677
Commercial paper	61	1,846
	2,005	4,209

24 Assets held for sale

	2006 £m	2005 £m
Land and buildings	8	1
Plant, equipment and vehicles	1	1
Equity investments	3	–
	12	2

25 Trade and other payables

	2006 £m	2005 £m
Trade payables	865	819
Wages and salaries	718	804
Social security	104	102
Other payables	265	240
Deferred income	40	34
Customer return and rebate accruals	1,119	1,187
Other accruals	1,713	1,784
Derivative financial instruments	40	171
Dividends payable	7	6
	4,871	5,147

25 Trade and other payables continued

Customer return and rebate accruals are provided for by the Group at the point of sale in respect of the estimated rebates, discounts or allowances payable to customers, principally in the USA. Provisions are made at the time of sale but the actual amounts paid are based on claims made some time after the initial recognition of the sale. As the amounts are estimated they may not fully reflect the final outcome and the amounts are subject to change dependent upon, amongst other things, the types of buying group and product sales mix. The level of provision is reviewed and adjusted quarterly in the light of historical experience of actual rebates, discounts or allowances given and returns made and any changes in arrangements. Future events could cause the assumptions on which the provisions are based to change, which could affect the future results of the Group.

26 Pensions and other post-employment benefits

Pension and other post-employment costs	2006 £m	2005 £m	2004 £m
UK pension schemes	159	124	119
US pension schemes	35	41	44
Other overseas pensions schemes	91	83	74
Unfunded post-retirement healthcare schemes	91	100	92
Other post-employment costs	1	2	18
	377	350	347
Analysed as:			
Funded defined benefit/hybrid pension schemes	237	198	192
Unfunded defined benefit pension schemes	19	25	22
Unfunded post-retirement healthcare schemes	91	100	92
Defined benefit schemes	347	323	306
Defined contribution pension schemes	29	25	23
Other post-employment costs	1	2	18
	377	350	347

The costs of the defined benefit pension and post-retirement healthcare schemes are charged in the income statement as follows:

Cost of sales	74	71	68
Selling, general and administration	175	177	166
Research and development	98	75	72
	347	323	306

GSK entities operate pension arrangements which cover the Group's material obligations to provide pensions to retired employees. These arrangements have been developed in accordance with local practices in the countries concerned. Pension benefits can be provided by state schemes; by defined contribution schemes, whereby retirement benefits are determined by the value of funds arising from contributions paid in respect of each employee, or by defined benefit schemes, whereby retirement benefits are based on employee pensionable remuneration and length of service. Some 'hybrid' defined benefit schemes also include defined contribution sections.

Contributions to defined benefit schemes are determined in accordance with the advice of independent, professionally qualified actuaries. Pension costs of defined benefit schemes for accounting purposes have been assessed in accordance with independent actuarial advice, using the projected unit method. In certain countries pension benefits are provided on an unfunded basis, some administered by trustee companies. Liabilities are generally assessed annually in accordance with the advice of independent actuaries. Formal, independent, actuarial valuations of the Group's main plans are undertaken regularly, normally at least every three years.

The assets of funded schemes are generally held in separately administered trusts or are insured. Assets are invested in different classes in order to maintain a balance between risk and return. Investments are diversified to limit the financial effect of the failure of any individual investment. The long term, overall target asset allocation is 60% equities, 30% bonds and 10% property.

Actuarial movements in the year are recognised in full through the statement of recognised income and expense.

The UK discount rate is based on the iBoxx over 15 year AA index and the US discount rate is based on corporate bond yields which reflect the term of the expected benefit payments. The expected rate of return on bonds reflects the portfolio mix of index-linked, government and corporate bonds. An equity risk premium of between 3% and 4% is added to longer term government bond yields to give the expected rate of return on equities. Projected inflation rate and pension increases are long term predictions based on the yield gap between long term index-linked and fixed interest Gilts. In the UK, mortality rates are calculated using the PA92 standard mortality tables projected to 2006. Plan obligations are then increased by between 3% and 10%, depending on each individual scheme's mortality experience, to make allowance for future improvements in life expectancy. In the USA, mortality rates are calculated using the RP2000 fully generational table, projected using scale AA, with the white collar adjustment.

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continued

26 Pensions and other post-employment benefits continued

The average life expectancy assumed now for an individual at the age of 60 and projected to apply in 2026 for an individual then at the age of 60 is as follows:

	UK		USA	
	Male Years	Female Years	Male Years	Female Years
Current	25.3	26.8	24.3	26.1
Projected for 2026	26.9	28.6	25.8	27.0

These mortality assumptions were set following a review in December 2005. GSK expects to review these again in December 2007.

During 2006, the Group made special funding contributions to the UK and US pension schemes totalling £346 million (2005 – £366 million). In 2006, GSK formalised an agreement with the trustees of the UK defined benefit pension schemes to make additional contributions of up to £325 million per year in addition to the normal contributions, over a four-year period ending 31st December 2009 in order to eliminate the then pension deficits on an IAS 19 basis.

In the UK the defined benefit pension schemes operated for the benefit of former Glaxo Wellcome employees and former SmithKline Beecham employees remain separate. These schemes were closed to new entrants in 2001 and subsequent UK employees are entitled to join a defined contribution scheme. In the USA the former Glaxo Wellcome and SmithKline Beecham defined benefit schemes were merged during 2001. In addition, the Group operates a number of post-retirement healthcare schemes, the principal one of which is in the USA.

The Group has applied the following financial assumptions in assessing the defined benefit liabilities:

	UK			USA			Rest of World		
	2006 % pa	2005 % pa	2004 % pa	2006 % pa	2005 % pa	2004 % pa	2006 % pa	2005 % pa	2004 % pa
Rate of increase of future earnings	4.25	4.00	4.00	5.00	5.00	5.00	3.25	3.25	3.25
Discount rate	5.00	4.75	5.25	5.75	5.50	5.75	4.25	3.75	4.25
Expected pension increases	3.00	2.75	2.50	n/a	n/a	n/a	2.00	2.00	2.00
Cash balance credit/conversion rate	n/a	n/a	n/a	4.75	4.50	4.75	1.75	1.75	1.75
Inflation rate	3.00	2.75	2.50	2.50	2.50	2.50	1.75	1.75	1.75

The amounts recorded in the income statement and statement of recognised income and expense for the three years ended 31st December 2006 in relation to the defined benefit pension and post-retirement healthcare schemes were as follows:

2006				Pensions	Post-retirement benefits
	UK £m	USA £m	Rest of World £m	Group £m	Group £m
Amounts charged to operating profit					
Current service cost	135	66	56	257	48
Past service cost	33	–	(2)	31	–
Expected return on pension scheme assets	(333)	(142)	(30)	(505)	–
Interest on scheme liabilities	307	113	42	462	57
Settlements and curtailments	17	(2)	(4)	11	(14)
	159	35	62	256	91
Actuarial gains recorded in the statement of recognised income and expense	111	169	10	290	139
2005					
Amounts charged to operating profit					
Current service cost	117	63	52	232	46
Past service cost	–	–	–	–	1
Expected return on pension scheme assets	(285)	(126)	(28)	(439)	–
Interest on scheme liabilities	276	104	34	414	53
Settlements and curtailments	16	–	–	16	–
	124	41	58	223	100
Actuarial losses recorded in the statement of recognised income and expense	(490)	(109)	(93)	(692)	(102)

26 Pensions and other post-employment benefits continued

2004	Pensions				Post-retirement benefits
	UK £m	USA £m	Rest of World £m	Group £m	Group £m
Amounts charged to operating profit					
Current service cost	117	58	42	217	37
Past service cost	–	–	2	2	–
Expected return on pension scheme assets	(272)	(118)	(20)	(410)	–
Interest on scheme liabilities	269	104	27	400	55
Settlements and curtailments	5	–	–	5	–
	119	44	51	214	92
Actuarial gains/(losses) recorded in the statement of recognised income and expense	162	26	(26)	162	(54)

The total actuarial losses recorded in the statement of recognised income and expense since 1st January 2003 amount to £689 million.

The fair values of the assets and liabilities of the UK and US defined benefit pension schemes, together with aggregated data for other defined benefit pension schemes in the Group are as follows:

At 31st December 2006	UK		USA		Rest of World		Group
	Expected rate of return %	Fair value £m	Expected rate of return %	Fair value £m	Average expected rate of return %	Fair value £m	Fair value £m
Equities	8.00	4,218	8.50	1,412	7.25	205	5,835
Property	7.00	210	7.50	169	6.75	11	390
Bonds	4.50	2,026	5.50	324	3.50	351	2,701
Other assets	5.00	100	5.00	48	3.75	174	322
Fair value of assets		6,554		1,953		741	9,248
Present value of scheme obligations		(7,444)		(1,949)		(952)	(10,345)
		(890)		4		(211)	(1,097)
Included in other non-current assets		–		160		19	179
Included in pensions and other post-employment benefits		(890)		(156)		(230)	(1,276)
		(890)		4		(211)	(1,097)
Actual return on plan assets		560		310		56	926
At 31st December 2005	UK		USA		Rest of World		Group
	Expected rate of return %	Fair value £m	Expected rate of return %	Fair value £m	Average expected rate of return %	Fair value £m	Fair value £m
Equities	7.75	3,895	8.50	1,440	7.00	192	5,527
Property	–	–	7.50	106	6.25	11	117
Bonds	4.25	1,764	5.50	352	3.50	302	2,418
Other assets	4.00	85	4.00	78	3.25	152	315
Fair value of assets		5,744		1,976		657	8,377
Present value of scheme obligations		(7,054)		(2,150)		(922)	(10,126)
		(1,310)		(174)		(265)	(1,749)
Included in other non-current assets		–		–		12	12
Included in pensions and other post-employment benefits		(1,310)		(174)		(277)	(1,761)
		(1,310)		(174)		(265)	(1,749)
Actual return on plan assets		932		129		63	1,124

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26 Pensions and other post-employment benefits continued

At 31st December 2004	UK		USA		Rest of World		Group
	Expected rate of return %	Fair value £m	Expected rate of return %	Fair value £m	Average expected rate of return %	Fair value £m	Fair value £m
Equities	8.25	3,053	8.50	1,223	7.50	208	4,484
Property	–	–	6.50	58	6.25	7	65
Bonds	4.50	1,428	5.75	307	3.75	270	2,005
Other assets	4.00	80	2.50	50	2.25	62	192
Fair value of assets		4,561		1,638		547	6,746
Present value of scheme obligations		(5,735)		(1,750)		(761)	(8,246)
		(1,174)		(112)		(214)	(1,500)
Included in other non-current assets		–		–		14	14
Included in pensions and other post-employment benefits		(1,174)		(112)		(228)	(1,514)
		(1,174)		(112)		(214)	(1,500)
Actual return on plan assets		468		204		43	715

Movements in defined benefit obligations	Pensions				Post-retirement benefits
	UK £m	USA £m	Rest of World £m	Group £m	Group £m
Obligations at 1st January 2004	(5,508)	(1,751)	(707)	(7,966)	(951)
Exchange adjustments	–	126	31	157	52
Service cost	(117)	(58)	(44)	(219)	(37)
Interest cost	(269)	(104)	(27)	(400)	(55)
Settlements and curtailments	(5)	–	–	(5)	–
Actuarial losses	(34)	(60)	(49)	(143)	(54)
Scheme participants' contributions	(12)	–	(3)	(15)	(8)
Benefits paid	210	97	38	345	48
Obligations at 31st December 2004	(5,735)	(1,750)	(761)	(8,246)	(1,005)
Exchange adjustments	–	(217)	14	(203)	(138)
Service cost	(117)	(63)	(52)	(232)	(47)
Interest cost	(276)	(104)	(34)	(414)	(53)
Settlements and curtailments	(16)	–	–	(16)	–
Actuarial losses	(1,137)	(112)	(128)	(1,377)	(102)
Scheme participants' contributions	(12)	–	(3)	(15)	(9)
Benefits paid	239	96	42	377	46
Obligations at 31st December 2005	(7,054)	(2,150)	(922)	(10,126)	(1,308)
Exchange adjustments	–	267	30	297	151
Service cost	(168)	(66)	(54)	(288)	(48)
Interest cost	(307)	(113)	(42)	(462)	(57)
Settlements and curtailments	(17)	2	12	(3)	14
Actuarial (losses)/gains	(116)	1	(16)	(131)	139
Scheme participants' contributions	(11)	–	(3)	(14)	(8)
Benefits paid	229	110	43	382	54
Obligations at 31st December 2006	(7,444)	(1,949)	(952)	(10,345)	(1,063)

The liability for the US post-retirement healthcare scheme has been assessed using the same assumptions as for the US pension scheme, together with the assumption for future medical inflation of 9.25%, reducing by 0.75% per year to 5% in 2013 and thereafter. On this basis the liability for the US scheme has been assessed at £927 million (2005 – £1,133 million, 2004 – £895 million).

26 Pensions and other post-employment benefits continued

The defined benefit pension obligation is analysed as follows:

	2006 £m	2005 £m	2004 £m
Funded	(10,099)	(9,858)	(8,029)
Unfunded	(246)	(268)	(217)
	(10,345)	(10,126)	(8,246)

Post-retirement benefits are unfunded.

Movements in fair value of assets	Pensions				Post-retirement benefits
	UK £m	USA £m	Rest of World £m	Group £m	Group £m
Assets at 1st January 2004	3,955	1,583	444	5,982	–
Exchange adjustments	–	(117)	27	(90)	–
Expected return on assets	272	118	20	410	–
Actuarial gains	196	86	23	305	–
Employer contributions	336	65	68	469	40
Scheme participants' contributions	12	–	3	15	8
Benefits paid	(210)	(97)	(38)	(345)	(48)
Assets at 31st December 2004	4,561	1,638	547	6,746	–
Exchange adjustments	–	200	(4)	196	–
Expected return on assets	285	126	28	439	–
Actuarial gains	647	3	35	685	–
Employer contributions	478	105	90	673	37
Scheme participants' contributions	12	–	3	15	9
Benefits paid	(239)	(96)	(42)	(377)	(46)
Assets at 31st December 2005	5,744	1,976	657	8,377	–
Exchange adjustments	–	(255)	(30)	(285)	–
Expected return on assets	333	142	30	505	–
Settlements and curtailments	–	–	(8)	(8)	–
Actuarial gains	227	168	26	421	–
Employer contributions	468	32	106	606	46
Scheme participants' contributions	11	–	3	14	8
Benefits paid	(229)	(110)	(43)	(382)	(54)
Assets at 31st December 2006	6,554	1,953	741	9,248	–

The UK defined benefit schemes include defined contribution sections with account balances totalling £609 million at 31st December 2006 (2005 – £515 million, 2004 – £404 million). Information on scheme assets under US GAAP is given in Note 41.

Employer contributions for 2007 are estimated to be approximately £500 million in respect of defined benefit pension schemes and £50 million in respect of post-retirement benefits.

The transition date for conversion to IFRS for GSK was 1st January 2003 and therefore the following historical data has been presented from that date. This will be built up to a rolling five year record next year.

History of experience gains and losses	Pensions				Post-retirement benefits
	UK £m	USA £m	Rest of World £m	Group £m	Group £m
2006					
Experience gains of scheme assets (£m)	227	168	26	421	
Percentage of scheme assets at 31st December 2006	3%	9%	4%	5%	
Experience (losses)/gains of scheme liabilities (£m)	(37)	(16)	(42)	(95)	17
Percentage of scheme obligations at 31st December 2006	–	1%	4%	1%	2%
Fair value of assets	6,554	1,953	741	9,248	–
Present value of scheme obligations	(7,444)	(1,949)	(952)	(10,345)	(1,063)
(Deficits)/surpluses in the schemes	(890)	4	(211)	(1,097)	(1,063)

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26 Pensions and other post-employment benefits continued

History of experience gains and losses	Pensions				Post-retirement benefits
	UK £m	USA £m	Rest of World £m	Group £m	Group £m
2005					
Experience gains of scheme assets (£m)	647	3	35	685	
Percentage of scheme assets at 31st December 2005	11%	–	5%	8%	
Experience losses of scheme liabilities (£m)	(94)	(10)	(35)	(139)	(4)
Percentage of scheme obligations at 31st December 2005	1%	–	4%	1%	–
Fair value of assets	5,744	1,976	657	8,377	–
Present value of scheme obligations	(7,054)	(2,150)	(922)	(10,126)	(1,308)
Deficits in the schemes	(1,310)	(174)	(265)	(1,749)	(1,308)
2004					
Experience gains of scheme assets (£m)	196	86	23	305	
Percentage of scheme assets at 31st December 2004	4%	5%	4%	5%	
Experience (losses)/gains of scheme liabilities (£m)	(25)	(5)	(18)	(48)	47
Percentage of scheme obligations at 31st December 2004	–	–	2%	1%	5%
Fair value of assets	4,561	1,638	547	6,746	–
Present value of scheme obligations	(5,735)	(1,750)	(761)	(8,246)	(1,005)
Deficits in the schemes	(1,174)	(112)	(214)	(1,500)	(1,005)
2003					
Experience gains of scheme assets (£m)	336	231	33	600	
Percentage of scheme assets at 31st December 2003	8%	15%	7%	10%	
Experience (losses)/gains of scheme liabilities (£m)	(183)	5	(19)	(197)	(123)
Percentage of scheme obligations at 31st December 2003	3%	–	3%	2%	13%
Fair value of assets	3,955	1,583	444	5,982	–
Present value of scheme obligations	(5,508)	(1,751)	(707)	(7,966)	(951)
Deficits in the schemes	(1,553)	(168)	(263)	(1,984)	(951)

Sensitivity analysis

Effect of changes in assumptions used on the annual defined benefit pension and post-retirement costs or the benefit obligations:

	£m
A 0.25% decrease in discount rate would have the following approximate effect:	
Increase in annual pension cost	4
Increase in annual post-retirement benefits cost	1
Increase in pension obligation	369
Increase in post-retirement benefits obligation	37
A one year increase in life expectancy would have the following approximate effect:	
Increase in annual pension cost	17
Increase in annual post-retirement benefits cost	3
Increase in pension obligation	259
Increase in post-retirement benefits obligation	39

26 Pensions and other post-employment benefits continued**Sensitivity analysis**

	£m
A 0.25% decrease in expected rates of returns on assets would have the following approximate effect:	
Increase in annual pension cost	22
A 1% increase in the rate of future healthcare inflation would have the following approximate effect:	
Increase in annual post-retirement benefits cost	8
Increase in post-retirement benefits obligation	89
A 0.25% increase in inflation would have the following approximate effect:	
Increase in annual pension cost	23
Increase in pension obligation	298

27 Other provisions

	Exchange Offer Incentive £m	Merger integration £m	Operational excellence £m	Legal and other disputes £m	Other provisions £m	Total £m
At 1st January 2006	133	59	52	1,165	227	1,636
Exchange adjustments	(5)	(1)	(5)	(94)	(15)	(120)
(Credit)/charge for the year	(2)	(24)	134	293	45	446
Unwinding of discount	2	–	–	24	10	36
Applied	(11)	(15)	(50)	(274)	(41)	(391)
Reversed unused	–	–	–	(8)	(14)	(22)
Reclassifications and other movements	–	(2)	–	(1)	1	(2)
At 31st December 2006	117	17	131	1,105	213	1,583
To be settled within one year	64	15	117	743	116	1,055
To be settled after one year	53	2	14	362	97	528
At 31st December 2006	117	17	131	1,105	213	1,583

The Group has recognised costs in previous years in respect of plans for the integration of the Glaxo Wellcome and SmithKline Beecham businesses. Implementation of the integration following the merger is substantially complete. The exchange offer incentive programme operated at the time of the merger to encourage staff to convert Glaxo Wellcome or SmithKline Beecham share options into GlaxoSmithKline share options. The incentive is paid either when employees exercise the relevant options, or when the options lapse, up to 2010. The discount on this provision increased by £2 million in 2006 (2005 – £4 million), and was calculated using risk-free rates of return. Costs recognised in the remaining merger integration provision in respect of identified severances are expected to be incurred in 2007.

Operational excellence is the term used by the Group to refer to the continuous worldwide programme of cost saving measures that are carried out within all areas of the business. The majority of these projects are of a short-term nature.

GSK is involved in a number of legal and other disputes, including notification of possible claims, as set out in Note 43 'Legal proceedings'. Provisions for legal and other disputes include amounts relating to US anti-trust, product liability, contract terminations, self-insurance, environmental clean-up and property rental. The company's Directors, having taken legal and other specialist advice, have established provisions after taking into account insurance and other agreements and having regard to the relevant facts and circumstances of each matter and in accordance with accounting requirements. These provisions were discounted by £2 million in 2006 (2005 – £71 million) using risk-adjusted projected cash flows and risk-free rates of return. The effect of the change in the discount rate in 2006 is to increase the discount at 31st December by £7 million. A number of products have a history of claims made and settlements which makes it possible to use an IBNR (incurred but not reported) actuarial technique to determine a reasonable estimate of the Group's exposure for unasserted claims in relation to those products. Apart from the IBNR provision, no provisions have been made for unasserted claims. The ultimate liability for such matters may vary from the amounts provided and is dependent upon the outcome of litigation proceedings, investigations and possible settlement negotiations.

It is in the nature of the Group's business that a number of these matters, including those provided using the IBNR actuarial technique, may be the subject of negotiation and litigation over several years. The largest individual amounts provided are expected to be settled within three years.

At 31st December 2006, it is expected that £120 million (2005 – £115 million) of the provision made for legal and other disputes will be reimbursed by third party insurers. This amount is included within current and non-current assets.

For a discussion of legal issues, refer to Note 43 'Legal proceedings'.

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28 Other non-current liabilities

	2006 £m	2005 £m
Accruals and deferred income	97	58
Derivative financial instruments	60	26
Other payables	249	383
	406	467

29 Contingent liabilities

At 31st December 2006 contingent liabilities, comprising guarantees, letters of credit, discounted bills and other items arising in the normal course of business, amounted to £258 million (2005 – £342 million). At 31st December 2006, £114 million (2005 – £96 million) of financial assets were pledged as collateral for contingent liabilities. For discussions of tax and legal issues, refer to Note 12, 'Taxation' and Note 43, 'Legal proceedings'.

30 Net debt

	2006 £m	2005 £m
Current assets:		
Liquid investments	1,035	1,025
Cash and cash equivalents	2,005	4,209
	3,040	5,234
Short-term borrowings:		
6.125% US\$ Notes 2006	–	(291)
2.375% US\$ Medium Term Note 2007	(255)	–
Commercial paper	–	(576)
Bank loans and overdrafts	(410)	(249)
Other loans	(11)	(46)
Obligations under finance leases	(42)	(38)
	(718)	(1,200)
Long-term borrowings:		
2.375% US\$ US Medium Term Note 2007	–	(283)
3.375% € European Medium Term Note 2008	(671)	(689)
4.875% £ European Medium Term Note 2008	(494)	(502)
3.25% € European Medium Term Note 2009	(338)	(342)
3.00% € European Medium Term Note 2012	(503)	(510)
4.375% US\$ US Medium Term Note 2014	(719)	(825)
4.00% € European Medium Term Note 2025	(497)	(503)
5.25% £ European Medium Term Note 2033	(977)	(976)
5.375% US\$ US Medium Term Note 2034	(253)	(288)
Loan stock	(10)	(11)
Bank loans	(1)	(3)
Other loans and private financing	(212)	(256)
Obligations under finance leases	(97)	(83)
	(4,772)	(5,271)
Net debt	(2,450)	(1,237)

Current assets

Liquid investments are classified as available-for-sale investments. At 31st December 2006, they included redeemable shares, which were fully collateralised with highly rated bonds, of € 1 billion (£676 million), and government bonds. The effective interest rate on liquid investments at 31st December 2006 was approximately 3.7% (2005 – approximately 2.8%).

The effective interest rate on cash and cash equivalents at 31st December 2006 was approximately 4.8% (2005 – approximately 4.0%).

30 Net debt continued**Short-term borrowings**

Commercial paper comprises a US\$10 billion programme, of which none was in issue at 31st December 2006 (2005 – \$991 million (£576 million)), backed up by committed facilities of 364 days duration of \$900 million (£459 million) (2005 – \$900 million (£523 million)) renewable annually, and liquid investments, cash and cash equivalents as shown in the table above.

The weighted average interest rate on current bank loans and overdrafts at 31st December 2006 was 2.4% (2005 – 4.0%).

Long-term borrowings

Loans due after one year are repayable over various periods as follows:

	2006 £m	2005 £m
Between one and two years	1,202	317
Between two and three years	366	1,224
Between three and four years	26	354
Between four and five years	7	9
After five years	3,171	3,367
	4,772	5,271

The loans repayable after five years carry interest at effective rates between 3.0% and 5.4%. The repayment dates range from 2012 to 2034.

The average effective interest rate of all Notes at 31st December 2006 was approximately 4.3% (2005 – approximately 4.5%).

Secured loans

Loans amounting to £8 million (2005 – £20 million) are secured by charges on non-current and current assets.

Finance lease obligations

	2006 £m	2005 £m
Rental payments due within one year	49	41
Rental payments due between one and two years	41	33
Rental payments due between two and three years	30	23
Rental payments due between three and four years	18	13
Rental payments due between four and five years	8	9
Rental payments due after five years	14	15
Total future rental payments	160	134
Future finance charges	(21)	(13)
Total finance lease obligations	139	121

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continued

31 Share capital and share premium account

	Ordinary shares of 25p each		Share premium
	Number	£m	£m
Share capital authorised			
At 31st December 2004	10,000,000,000	2,500	
At 31st December 2005	10,000,000,000	2,500	
At 31st December 2006	10,000,000,000	2,500	
Share capital issued and fully paid			
At 1st January 2004	5,949,463,628	1,487	264
Issued under share option schemes	6,300,203	2	40
Purchased and cancelled	(18,075,000)	(5)	–
At 31st December 2004	5,937,688,831	1,484	304
Issued under share option schemes	25,162,425	7	245
At 31st December 2005	5,962,851,256	1,491	549
Issued under share option schemes	28,750,592	7	309
At 31st December 2006	5,991,601,848	1,498	858

	31st December 2006	31st December 2005	31st December 2004
Number ('000) of shares issuable under outstanding options (Note 40)	225,163	221,293	276,954
Number ('000) of unissued shares not under option	3,783,235	3,815,856	3,785,358

At 31st December 2006, of the issued share capital, 153,451,642 shares were held in the ESOP Trust, 235,482,678 shares were held as Treasury shares and 5,602,667,528 shares were in free issue. All issued shares are fully paid. The nominal, carrying and market values of the shares held in the ESOP Trust are disclosed in Note 40.

In October 2006, the Group announced a new share buy-back programme totalling £6 billion, which is expected to be completed over a three year period. The exact amount and timing of future purchases, and the extent to which repurchased shares will be held as Treasury shares rather than being cancelled, will be determined by the company and is dependent on market conditions and other factors. In 2006, the Group also commenced close period share buy-backs by operating under specific, irrevocable agreements put in place with its brokers prior to the start of each close period.

A total of £7.8 billion has been spent by the company between 1st January 2001 and 31st December 2006 on buying its own shares for cancellation or to be held as Treasury shares, of which £1.3 billion was spent in 2006 (£0.5 billion under the new £6 billion programme).

20.4 million shares have been purchased in the period 1st January 2007 to 23rd February 2007 at a cost of £290 million. All purchases were made through the publicly announced buy-back programme.

The table below sets out the monthly purchases under the share buy-back programme:

Month	Number of shares 000	Average share price excluding commission and stamp duty £
January 2006	Nil	–
February 2006	4,375	14.67
March 2006	10,040	15.34
April 2006	640	15.63
May 2006	10,200	15.09
June 2006	8,567	14.81
July 2006	5,935	15.07
August 2006	9,080	14.41
September 2006	6,525	14.42
October 2006	10,628	14.30
November 2006	18,550	13.73
December 2006	8,163	13.39
Total	92,703	14.45

All shares purchased in 2006 are held as Treasury shares. For details of substantial shareholdings refer to 'Substantial shareholdings' on page 183.

32 Movements in equity

	Shareholders' equity					Minority interests £m	Total equity £m
	Share capital £m	Share premium £m	Retained earnings £m	Other reserves £m	Total £m		
At 1st January 2004	1,487	264	3,959	(793)	4,917	681	5,598
Recognised income and expense for the year	–	–	3,906	–	3,906	93	3,999
Changes in minority shareholdings	–	–	–	–	–	(489)	(489)
Distributions to minority shareholders	–	–	–	–	–	(72)	(72)
Dividends to shareholders	–	–	(2,476)	–	(2,476)	–	(2,476)
Ordinary shares issued	2	40	–	–	42	–	42
Ordinary shares purchased and cancelled	(5)	–	(201)	5	(201)	–	(201)
Ordinary shares purchased and held as Treasury shares	–	–	(799)	–	(799)	–	(799)
Ordinary shares transferred by ESOP Trusts	–	–	–	23	23	–	23
Write-down of shares held by ESOP Trusts	–	–	(180)	180	–	–	–
Share-based incentive plans	–	–	333	(21)	312	–	312
At 31st December 2004	1,484	304	4,542	(606)	5,724	213	5,937
Implementation of accounting for financial instruments under IAS 39	–	–	(94)	78	(16)	4	(12)
At 1st January 2005, as adjusted	1,484	304	4,448	(528)	5,708	217	5,925
Recognised income and expense for the year	–	–	4,426	(3)	4,423	153	4,576
Changes in minority shareholdings	–	–	(15)	–	(15)	(25)	(40)
Distributions to minority shareholders	–	–	–	–	–	(86)	(86)
Dividends to shareholders	–	–	(2,390)	–	(2,390)	–	(2,390)
Ordinary shares issued	7	245	–	–	252	–	252
Ordinary shares purchased and held as Treasury shares	–	–	(1,000)	–	(1,000)	–	(1,000)
Ordinary shares transferred by ESOP Trusts	–	–	–	68	68	–	68
Write-down of shares held by ESOP Trusts	–	–	(155)	155	–	–	–
Share-based incentive plans	–	–	240	–	240	–	240
Tax on share-based incentive plans	–	–	25	–	25	–	25
At 31st December 2005	1,491	549	5,579	(308)	7,311	259	7,570
Recognised income and expense for the year	–	–	5,248	59	5,307	88	5,395
Changes in minority shareholdings	–	–	–	–	–	2	2
Distributions to minority shareholders	–	–	–	–	–	(87)	(87)
Dividends to shareholders	–	–	(2,598)	–	(2,598)	–	(2,598)
Ordinary shares issued	7	309	–	–	316	–	316
Ordinary shares purchased and held as Treasury shares	–	–	(1,348)	–	(1,348)	–	(1,348)
Ordinary shares transferred by ESOP Trusts	–	–	–	151	151	–	151
Write-down of shares held by ESOP Trusts	–	–	(163)	163	–	–	–
Share-based incentive plans	–	–	226	–	226	–	226
Tax on share-based incentive plans	–	–	21	–	21	–	21
At 31st December 2006	1,498	858	6,965	65	9,386	262	9,648

Retained earnings and other reserves amounted to £7,030 million at 31st December 2006 (2005 – £5,271 million, 2004 – £3,936 million) of which £7,180 million (2005 – £8,067 million, 2004 – £10,243 million) relates to the company and £185 million (2005 – £180 million, 2004 – £108 million) relates to joint ventures and associated undertakings. The cumulative translation exchange in equity since 1st January 2003 is shown in the following table:

	2006 £m	2005 £m	2004 £m
Translation exchange at 1st January	217	5	46
Exchange movements on overseas net assets	(390)	203	(47)
Exchange movements on goodwill in reserves	31	9	6
Translation exchange at 31st December	(142)	217	5

Notes to the financial statements

continued

32 Movements in equity continued

Other reserves is analysed as follows:

	ESOP Trust shares £m	Fair value reserve £m	Cash flow hedge reserve £m	Other reserves £m	Total £m
At 1st January 2004	(2,718)	–	–	1,925	(793)
Ordinary shares purchased and cancelled	–	–	–	5	5
Ordinary shares transferred by ESOP Trusts	23	–	–	–	23
Write-down of shares held by ESOP Trusts	180	–	–	–	180
Share-based incentive plans	(21)	–	–	–	(21)
At 31st December 2004	(2,536)	–	–	1,930	(606)
Implementation of accounting for financial instruments under IAS 39	–	76	2	–	78
At 1st January 2005, as adjusted	(2,536)	76	2	1,930	(528)
Recognised income and expense for the year	–	–	(3)	–	(3)
Ordinary shares transferred by ESOP Trusts	68	–	–	–	68
Write-down of shares held by ESOP Trusts	155	–	–	–	155
At 31st December 2005	(2,313)	76	(1)	1,930	(308)
Recognised income and expense for the year	–	61	(2)	–	59
Ordinary shares transferred by ESOP Trusts	151	–	–	–	151
Write-down of shares held by ESOP Trusts	163	–	–	–	163
At 31st December 2006	(1,999)	137	(3)	1,930	65

Other reserves include the merger reserve created on the merger of Glaxo Wellcome and SmithKline Beecham amounting to £1,561 million at 31st December 2006 (2005 – £1,561 million; 2004 – £1,561 million). Other reserves also include the capital redemption reserve created as a result of the share buy-back programme amounting to £81 million at 31st December 2006 (2005 – £81 million, 2004 – £81 million).

33 Related party transactions

GlaxoSmithKline held an 18.7% interest in Quest Diagnostics Inc. at 31st December 2006 (2005 – 18.4%). The Group and Quest Diagnostics are parties to a long-term contractual relationship under which Quest Diagnostics is the primary provider of clinical laboratory testing to support the Group's clinical trials testing requirements worldwide. During 2006, Quest Diagnostics provided services of £48 million (2005 – £39 million) to the Group. At 31st December 2006 the balance payable by GlaxoSmithKline to Quest Diagnostics was £4 million (2005 – £5 million).

In 2006, both the Group and Shionogi & Co. Ltd. entered into transactions with their 50/50 US joint venture company in support of the research and development activities conducted by that joint venture company. During 2006, GlaxoSmithKline provided services to the joint venture of £2 million (2005 – £1 million). At 31st December 2006 the balance due to GlaxoSmithKline from the joint venture was £3 million (2005 – £1 million).

Dr Shapiro, a former Non-Executive Director of GlaxoSmithKline plc, received fees of \$85,000 (2005 – \$85,000) of which \$30,000 (2005 – \$30,000) was in the form of ADSs, from a subsidiary of the company, for her membership of the Group's Scientific Advisory Board. These fees are included within 'Annual remuneration' in the Remuneration Report on pages 65 to 82.

The aggregate compensation of the Directors, CET and Company Secretary is given in Note 8, 'Employee Costs'.

34 Reconciliation of profit after tax to operating cash flows**Reconciliation of profit after tax to operating cash flows**

	Notes	2006 £m	2005 £m	2004 £m
Profit after tax	5	5,498	4,816	4,022
Tax on profits		2,301	1,916	1,757
Share of after tax profits of associates and joint ventures		(56)	(52)	(60)
Profit on disposal of interest in associates		–	–	(149)
Finance income/costs		65	194	186
Depreciation		732	710	691
Impairment and assets written off		208	193	94
Amortisation of intangible assets		226	194	168
(Profit)/loss on sale of property, plant and equipment		–	(19)	2
(Profit)/loss on sale of intangible assets		(158)	(203)	1
Profit on sale of equity investments		(18)	(15)	(33)
Fair value loss on inventory sold		–	–	13
Changes in working capital:				
(Increase)/decrease in inventories		(298)	47	(33)
Increase in trade and other receivables		(529)	(397)	(235)
Increase in trade and other payables		354	491	163
Decrease in pension and other provisions		(270)	(453)	(351)
Share-based incentive plans		226	236	333
Other		(78)	7	(42)
Cash generated from operations		8,203	7,665	6,527

35 Reconciliation of net cash flow to movement in net debt**Reconciliation of net cash flow to movement in net debt**

Net debt at beginning of year		(1,237)	(1,984)	(1,648)
Implementation of accounting for financial instruments under IAS 39		–	13	–
(Decrease)/increase in cash and bank overdrafts		(1,956)	1,384	617
Cash outflow/(inflow) from liquid investments		55	(550)	53
Net increase in long-term loans		–	(912)	(1,350)
Net repayment of short-term loans		739	857	407
Net repayment of obligations under finance leases		34	36	22
Net non-cash funds of subsidiary undertakings acquired		–	(68)	–
Exchange adjustments		(9)	39	24
Other non-cash movements		(76)	(52)	(109)
Movement in net debt		(1,213)	747	(336)
Net debt at end of year		(2,450)	(1,237)	(1,984)

Notes to the financial statements

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35 Reconciliation of net cash flow to movement in net debt continued

Analysis of changes in net debt	At 31.12.05 £m	Exchange £m	Other £m	Acquisitions £m	Cash flow £m	At 31.12.06 £m
Liquid investments	1,025	(45)	–	–	55	1,035
Cash and cash equivalents	4,209	(281)	–	25	(1,948)	2,005
Overdrafts	(237)	27	–	–	(33)	(243)
	3,972	(254)	–	25	(1,981)	1,762
Debt due within one year:						
Commercial paper	(576)	–	–	–	576	–
Eurobonds and Medium-Term Notes	(291)	10	(255)	–	281	(255)
Other	(96)	(1)	(11)	–	(112)	(220)
	(963)	9	(266)	–	745	(475)
Debt due after one year:						
Eurobonds, Medium-Term Notes and private financing	(5,160)	271	230	–	–	(4,659)
Other	(111)	10	(40)	–	28	(113)
	(5,271)	281	190	–	28	(4,772)
Net debt	(1,237)	(9)	(76)	25	(1,153)	(2,450)

For further information on significant changes in net debt see Note 30 'Net debt'.

36 Acquisitions and disposals

Details of the acquisition and disposal of subsidiary and associated undertakings, joint ventures and other businesses are given below:

2006

Acquisitions

CNS, Inc.

On 19th December 2006, the Group acquired 100% of the issued share capital of CNS, Inc., a consumer healthcare company based in the USA for a cash consideration of £280 million. The company markets *Breathe Right* nasal dilator strips and *FiberChoice* dietary fibre supplements. These are the key intangible assets acquired and have been valued using a discounted cash flow calculation. This transaction has been accounted for by the purchase method of accounting. The goodwill arising on the acquisition reflects the potential for expansion of the brands into other overseas markets and the expected synergies for the Group. CNS, Inc. had a turnover of £71 million (2005 – £60 million) and a profit of £11 million (2005 – profit £9 million) for the year of which £2 million of turnover and £nil of profit related to the period since acquisition and are included in the Group accounts.

	Book value £m	Fair value adjustment £m	Fair value £m
Net assets acquired			
Intangible assets	4	203	207
Property, plant and equipment	1	–	1
Other assets including cash and cash equivalents	44	–	44
Deferred tax provision	–	(77)	(77)
Other liabilities	(7)	–	(7)
	42	126	168
Goodwill	–	112	112
Total consideration	42	238	280

36 Acquisitions and disposals continued**Euclid SR Partners, LP**

During 2006, an additional £5 million was invested in Euclid SR Partners, LP, an associate in which the Group has a 38.7% share.

Shionogi-GlaxoSmithKline Holdings Ltd

During 2006, an additional £8 million was invested in Shionogi GlaxoSmithKline Holdings Ltd, a joint venture in which the Group has a 50% share.

Pliva Research Institute Ltd.

In May 2006, the Group purchased the entire share capital of the Pliva Research Institute Ltd. for a cash consideration of £26 million, of this amount £8 million is deferred, with payment being made when Phase I clinical trials are initiated.

GlaxoSmithKline K.K.

In August 2006, a Japanese subsidiary of the Group made a cash payment of £150 million to complete the purchase of the remaining 15% of the share capital held by the minority shareholder. This payment was preceded in the year by a dividend to the minority shareholders of £7 million representing additional consideration.

Cash flows	CNS Inc. £m	Euclid SR Partners, LP £m	Shionogi GlaxoSmithKline Holdings Ltd. £m	Pliva Research Institute £m	GlaxoSmith- Kline K.K. £m	Other £m	Total £m
Cash consideration	280	5	8	18	157	–	468
Cash and cash equivalents acquired	(24)	–	–	(1)	–	–	(25)
Net cash payment on acquisitions	256	5	8	17	157	–	443
Net cash proceeds from disposals	–	–	–	–	–	(5)	(5)

2005**Acquisitions****ID Biomedical Corporation**

On 8th December 2005, the Group acquired 100% of the issued share capital of ID Biomedical Corporation, a biotechnology company based in Canada specialising in the development and manufacture of vaccines, particularly influenza vaccines, for a cash consideration of £874 million. This transaction has been accounted for by the purchase method of accounting. The goodwill arising on the acquisition results from benefits which cannot be separately quantified and recorded, including immediate access to additional 'flu vaccines manufacturing capacity, particularly in the event of a pandemic, a skilled workforce and good relations with the US and Canadian governments regarding the supply of 'flu vaccines. ID Biomedical Corporation had a turnover of £30 million (2004 – £23 million) and a loss of £83 million (2004 – loss £17 million) for the year, of which £1 million of turnover and £11 million of loss related to the period since acquisition and are included in the Group accounts.

	Book value £m	Fair value adjustment £m	Fair value £m
Net assets acquired			
Intangible assets	15	686	701
Property, plant and equipment	88	–	88
Other assets	74	23	97
Deferred tax provision	–	(225)	(225)
Other liabilities	(136)	(8)	(144)
	41	476	517
Goodwill	–	357	357
Total consideration	41	833	874

The total consideration included directly attributable costs of £3 million.

Notes to the financial statements

continued

36 Acquisitions and disposals continued

Corixa Corporation

On 12th July 2005, the Group acquired 92% of the issued share capital of Corixa Corporation, a biotechnology company specialising in developing vaccine adjuvants and immunology based products, for a cash consideration of £150 million. This investment increased the Group's holding in Corixa to 100%. The Group had a number of business relationships with Corixa prior to the acquisition date, principally in relation to an adjuvant developed by Corixa and used in some of the Group's vaccines. This transaction has been accounted for by the purchase method of accounting. The existing 8% investment in Corixa, with a book value of £12 million, was previously classified as an available-for-sale investment and now forms part of the investment in the subsidiary. The existing 8% of the issued share capital had been acquired, in previous years, for a cash consideration of £24 million. Corixa Corporation had a turnover of £3 million and a loss of £49 million for the year, of which £1 million of turnover and £24 million of loss related to the period since acquisition and are included in the Group accounts.

	Book value £m	Fair value adjustment £m	Fair value £m
Net assets acquired			
Intangible assets	–	115	115
Other assets	91	29	120
Other liabilities	(95)	(4)	(99)
	(4)	140	136
Goodwill	–	26	26
Existing investment	(12)	–	(12)
Total consideration	(16)	166	150

The total consideration included directly attributable costs of £1 million.

Euclid SR Partners, LP

During 2005 an additional £2 million was invested in Euclid SR Partners, LP, an associate in which the Group has a 38.7% interest.

GlaxoSmithKline Consumer Healthcare Limited

In April 2005, an Indian subsidiary of the Group purchased 3.16% of the share capital held by minority shareholders, for a cash consideration of £16 million.

GlaxoSmithKline Pharmaceuticals Limited

In May and June 2005, an Indian subsidiary of the Group purchased 1.52% of the share capital held by minority shareholders, for a cash consideration of £26 million.

GlaxoSmithKline Biologicals (Shanghai) Limited

During 2005, a Chinese subsidiary of the Group purchased all of the share capital held by minority shareholders for a cash consideration of £4 million.

Disposals

Ideapharm SA

In December 2005, the Group disposed of Ideapharm SA, a subsidiary located in Romania, for cash proceeds of £3 million, which were received in January 2006. The net assets disposed of in the year included cash of £2 million.

Aseptic Technologies S.A.

In April 2005, the Group disposed of 16.22% of Aseptic Technologies S.A. to Societe Regionale d'Investissement de Wallonie S.A. for cash proceeds of £10 million.

Cash flows	GSK Biologicals (Shanghai) £m	Aseptic Tech. £m	GSK Pharma- ceuticals £m	GSK Consumer Healthcare £m	Ideapharm £m	Euclid SR £m	Corixa £m	ID Biomedical £m	Total
Cash consideration	4	–	26	16	–	2	150	874	1,072
Cash and cash equivalents acquired	–	–	–	–	–	–	(7)	9	2
Net cash payment on acquisitions	4	–	26	16	–	2	143	883	1,074
Cash and cash equivalents disposed	–	–	–	–	2	–	–	–	2
Net cash proceeds from disposals	–	10	–	–	–	–	–	–	10

36 Acquisitions and disposals continued**2004****Acquisitions***Fraxiparine, Fraxodi and Arixtra*

In September 2004, the Group acquired *Fraxiparine, Fraxodi and Arixtra* and related assets including a manufacturing facility for a cash consideration of £297 million.

	Book value £m	Fair value adjustment £m	Net assets acquired £m
Intangible assets	–	262	262
Tangible fixed assets	56	(24)	32
Inventory	79	–	79
Provisions for onerous contracts	–	(76)	(76)
	135	162	297

Euclid SR Partners, LP

During 2004 an additional £2 million was invested in Euclid SR Partners, LP, an associate company in which the Group has a 38.7% interest.

Disposals**Quest Diagnostics Inc.**

During 2004, the Group disposed of 3.8 million shares from its investment in Quest Diagnostics Inc. for cash proceeds of £188 million, reducing the Group's shareholding at 31st December 2004 to 18.6%. A profit of £150 million was recognised.

GlaxoSmithKline Vehicle Finance Ltd

During 2004, the Group disposed of its employee vehicle financing subsidiary resulting in a loss of £3 million.

GlaxoSmithKline Pharmaceuticals (Chongqing) Ltd

During 2004, the Group disposed of GlaxoSmithKline Pharmaceuticals (Chongqing) Ltd, a Group subsidiary located in China, for £7 million. A profit on disposal of £2 million was realised.

Beeyar Investments (Pty) Ltd

In July 2004, the Group disposed of Beeyar Investments (Pty) Ltd, a subsidiary located in South Africa, for cash proceeds of £1 million, realising a profit of £1 million.

OptiLead S.r.l.

During the year, part of the Group's holding in an associated undertaking, OptiLead S.r.l. was sold, resulting in a loss of £1 million.

Cash flows	<i>Fraxiparine Fraxodi and Arixtra</i> £m	Euclid SR £m	Quest Diagnostics £m	GSK Vehicle Finance £m	GSK Pharmaceuticals (Chongqing) £m	Beeyar Investments £m	Total £m
Cash consideration paid	297	2	–	–	–	–	299
Net cash proceeds from disposals	–	–	188	34	7	1	230

Notes to the financial statements

continued

37 Commitments

Contractual obligations and commitments	2006 £m	2005 £m
Contracted for but not provided in the financial statements:		
Intangible assets	3,219	1,833
Plant, property and equipment	521	376
Investments	196	13
Purchase commitments	299	376
Business combinations	258	–
Pensions	975	2,200
Theravance put option agreement	258	258
Other commitments	65	64
Interest on loans	2,875	3,067
	8,666	8,187

The commitments related to intangible assets include milestone payments, which are dependent on successful clinical development and which represent the maximum that would be paid if all milestones are achieved. A number of commitments were made in 2006 under licensing and other agreements, including ChemoCentryx Inc., EPIX Pharmaceuticals Inc. and Genmab A/S. At 31st December 2006, the Genmab agreement was subject to review by the US Government under the Hart-Scott-Rodino Act. Approval was received on 6th February 2007.

On 8th December 2006, GSK entered into an agreement to acquire Domantis Limited for £230 million in cash. At 31st December 2006, the acquisition agreement was subject to clearance under the Hart-Scott-Rodino Act. Approval was received on 5th January 2007. On 21st December 2006, GSK entered into an agreement to acquire all the outstanding shares of Praecis Pharmaceuticals Inc. for approximately \$54.8 million (£28 million) by means of a cash tender offer in early 2007.

In 2006, GSK formalised an agreement with the trustees of the UK pension schemes to make additional contributions of up to £325 million per year, in addition to the normal contributions, over a four-year period ending 31st December 2009 in order to eliminate the then pension deficits on an IAS 19 basis, by that point. The table above shows this commitment, but excludes the normal ongoing annual funding requirement of approximately £200 million. GSK has also committed to eliminate any future deficits that may arise over a rolling five-year period. No other commitments have been made past 31st December 2009.

The Group has entered into a put option agreement whereby Theravance's shareholders can sell up to half of their Theravance shares to GSK at a pre-determined price (\$19.375). Given the maximum number of shares subject to the put option, the Group's obligation is capped at \$525 million. The expiry date is August 2007.

The Group also has other commitments which principally relate to revenue payments to be made under licences and other alliances.

Commitments in respect of future interest payable on loans are disclosed after taking into account the effect of interest rate swaps.

Commitments under operating leases	2006 £m	2005 £m
Rental payments due within one year	94	111
Rental payments due between one and two years	74	78
Rental payments due between two and three years	55	60
Rental payments due between three and four years	41	45
Rental payments due between four and five years	33	40
Rental payments due after five years	77	103
Total commitments under operating leases	374	437

38 Post balance sheet events

On 5th January 2007, GSK completed the acquisition of Domantis Limited for £230 million in cash.

On 7th February 2007, the FDA approved orlistat for OTC use in the USA under the brand name *alli*.

On 15th February 2007, GSK entered into a second hedging contract over an additional 10 million shares in Quest Diagnostics Inc. through another series of variable sale forward contracts maturing between 2013 and 2015.

On 16th February 2007, GSK completed the cash tender offer for Praecis Pharmaceuticals Inc.

On 20th February 2007, GSK and the Roche Group settled their arbitration proceedings relating to the licensing and co-marketing of carvedilol and GSK acquired from Roche the OTC marketing rights to orlistat outside the USA.

39 Financial instruments and related disclosures

Financial risk management

GlaxoSmithKline plc reports in Sterling and pays dividends out of Sterling profits. The role of Corporate Treasury in GSK is to manage and monitor the Group's external and internal funding requirements and financial risks in support of Group corporate objectives. Treasury activities are governed by policies and procedures approved by the Board and monitored by a treasury management group.

GSK maintains treasury control systems and procedures to monitor foreign exchange, interest rate, liquidity, credit and other financial risks.

GSK uses a variety of financial instruments, including derivatives, to finance its operation and to manage market risks from these operations. Financial instruments include cash and liquid resources, borrowings and spot foreign exchange contracts.

A number of derivative financial instruments are used to manage the market risks from Treasury operations. Derivative instruments, principally comprising forward foreign currency contracts and interest rate and currency swaps, are used to swap borrowings and liquid assets into the currencies required for Group purposes and to manage exposure to funding risks from changes in foreign exchange rates and interest rates.

GSK balances the use of borrowings and liquid assets having regard to the cash flow from operating activities and the currencies in which it is earned; the tax cost of intra-Group distributions; the currencies in which business assets are denominated; and the post-tax cost of borrowings compared to the post-tax return on liquid assets.

Liquid assets surplus to the immediate operating requirements of Group companies are generally invested and managed centrally by Corporate Treasury. Requirements of Group companies for operating finance are met whenever possible from central resources.

External borrowings, mainly managed centrally by Corporate Treasury, comprise a portfolio of long and medium-term instruments and short-term finance.

GSK does not hold or issue derivative financial instruments for trading purposes and the Group's Treasury policies specifically prohibit such activity. All transactions in financial instruments are undertaken to manage the risks arising from underlying business activities, not for speculation.

Foreign exchange risk management

In GSK foreign currency transaction exposure arising on normal trade flows, in respect of both external and intra-Group trade, is not hedged. GSK's policy is to minimise the exposure of overseas operating subsidiaries to transaction risk by matching local currency income with local currency costs. For this purpose, intra-Group trading transactions are matched centrally and intra-Group payment terms are managed to reduce risk. Exceptional foreign currency cash flows are hedged selectively under the management of Corporate Treasury.

The Group seeks to denominate borrowings in the currencies of its principal assets and cash flows. These are primarily denominated in US Dollars, Euros and Sterling. Certain of these and other borrowings are swapped into other currencies as required for Group purposes.

Borrowings denominated in, or swapped into, foreign currencies that match investments in overseas Group assets are treated as a hedge against the relevant net assets.

At 31st December 2006, the Group had outstanding contracts to sell or purchase foreign currency having a total gross notional principal amount of £14,687 million (2005 – £15,974 million). The majority of contracts are for periods of 12 months or less.

Based on the composition of net debt at 31st December 2006, a 10% appreciation in Sterling against major currencies would result in a reduction in the Group's net debt of approximately £210 million. A 10% weakening in Sterling against major currencies would result in an increase in the Group's net debt of approximately £256 million.

Interest rate risk management

GSK's policy on interest rate risk management requires that the amount of net borrowings at fixed rates increases with the ratio of forecast net interest payable to trading profit.

The Group uses a limited number of interest rate swaps to redenominate external borrowings into the interest rate coupon required for Group purposes. The duration of these swaps matches the duration of the principal instruments. Interest rate derivative instruments are accounted for as fair value or cash flow hedges of the relevant assets or liabilities.

The Group manages centrally the short-term cash surpluses or borrowing requirements of subsidiary companies and uses forward contracts to hedge future repayments back into originating currency.

Sensitivity analysis considers the sensitivity of the Group's net debt to hypothetical changes in market rates and assumes that all other variables remain constant. Based on the composition of net debt and financing arrangements at 31st December 2006, and taking into consideration all fixed rate borrowings in place, a one percentage point (100 basis points) decrease in average interest rates would result in an increase in the Group's annual net interest charge of approximately £5 million.

Market risk of financial assets

The Group invests centrally managed liquid assets in government bonds, short-term corporate debt instruments with a minimum short-term credit rating of A-1/P-1, money market funds with a credit rating of AAA/Aaa and other structured investments (credit ratings shown are from Standard and Poor's and Moody's Investors' Services, respectively). These investments are classified as available-for-sale.

Equity investments are classified as available-for-sale investments and the Group manages disposals to meet overall business requirements as they arise. The Group regularly monitors the value of its equity investments and only enters into hedges selectively with the approval of the Board.

Credit risk

In the USA, in line with other pharmaceutical companies, the Group sells its products through a small number of wholesalers in addition to hospitals, pharmacies, physicians and other groups. Sales to the three largest wholesalers amounted to approximately 80% of the Group's US pharmaceutical sales. At 31st December 2006, the Group had trade receivables due from these three wholesalers totalling £1,044 million (31st December 2005 – £1,051 million).

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39 Financial instruments and related disclosures continued

The Group is exposed to a concentration of credit risk in respect of these wholesalers such that, if one or more of them is affected by financial difficulty, it could materially and adversely affect the Group's financial results.

The Group does not believe it is exposed to major concentrations of credit risk on other classes of financial instruments. The Group is exposed to credit-related losses in the event of non-performance by counterparties to financial instruments, but does not expect any counterparties to fail to meet their obligations. Where the Group has significant investments with a single counterparty, collateral is obtained in order to reduce risk.

The Group applies Board-approved limits to the amount of credit exposure to any one counterparty and employs strict minimum credit worthiness criteria as to the choice of counterparty.

Liquidity

The Group operates globally, primarily through subsidiary companies established in the markets in which the Group trades. Due to the nature of the Group's business with patent protection on many products in the Group's portfolio, the Group's products compete largely on product efficacy rather than on price. Selling margins are sufficient to exceed normal operating costs and the Group's operating subsidiaries are substantially cash generative.

Operating cash flow is used to fund investment in the research and development of new products as well as routine outflows of capital expenditure, tax, dividends and repayment of maturing debt. The Group may, from time to time, have additional demands for finance, such as for share purchases and business acquisitions.

GSK operates with a high level of interest cover and at low levels of net debt relative to its market capitalisation. In addition to the strong positive cash flow from normal trading activities, additional liquidity is readily available via its commercial paper programme and short-term investments. The Group also has a European Medium Term Note programme of £10 billion, of which £3.5 billion was in issue at 31st December 2006. In March 2004, the Group established a US Shelf Registration of \$5 billion; at 31st December 2006 \$2.4 billion (£1.2 billion) was in issue.

Fair value of financial assets and liabilities

The table on page 129 presents the carrying amounts under IFRS and the fair values of the Group's financial assets and liabilities at 31st December 2006 and 31st December 2005.

The fair values of the financial assets and liabilities are included at the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The following methods and assumptions were used to estimate the fair values:

- Equity investments – investments traded in an active market, determined by reference to the relevant stock exchange quoted bid price; other investments determined by reference to the current market value of similar instruments or by reference to the discounted cash flows of the underlying net assets

- Cash and cash equivalents – approximates to the carrying amount
- Liquid investments – based on quoted market prices in the case of marketable securities; based on principal amounts in the case of non-marketable securities because of their short repricing periods
- Short-term loans and overdrafts – approximates to the carrying amount because of the short maturity of these instruments
- Long-term loans – based on quoted market prices in the case of the Eurobonds and other fixed rate borrowings; approximates to the carrying amount in the case of floating rate bank loans and other loans
- Forward exchange contracts – based on market prices and exchange rates at the balance sheet date
- Currency swaps – based on market valuations at the balance sheet date
- Quest equity collar and Theravance put and call options – based on an option pricing model which uses significant assumptions in respect of price volatility, dividend yield and interest rates
- Interest rate instruments – based on the net present value of discounted cash flows
- Receivables and payables – approximates to the carrying amount
- Lease obligations – approximates to the carrying amount.

In the year ended 31st December 2006, the total amount of the change in fair values estimated using valuation techniques referred to above resulted in a credit to the income statement of £5 million (2005 – £1 million).

Fair value of investments in GSK shares

At 31st December 2006 the ESOP Trusts held GSK ordinary shares with a carrying value of £1,999 million (2005 – £2,313 million) with a fair value of £2,062 million (2005 – £2,460 million) based on quoted market price. The shares represent purchases by the ESOP Trusts to satisfy future exercises of options and awards under employee incentive schemes. The carrying value, which is the lower of cost or expected proceeds, of these shares has been recognised as a deduction from other reserves. At 31st December 2006, GSK held Treasury shares at a cost of £3,147 million (2005 – £1,799 million) which has been deducted from retained earnings.

Committed facilities

The Group has committed facilities to back up the commercial paper programme of \$900 million (£459 million) (2005 – \$900 million (£523 million)) of 364 days duration, renewable annually. At 31st December 2006, undrawn committed facilities totalled \$900 million (£459 million) (2005 – \$900 million (£523 million)).

39 Financial instruments and related disclosures continued**Classification and fair values of financial assets and liabilities**

The following table sets out the classification of financial assets and liabilities. Receivables and payables have been included to the extent they are classified as financial assets and liabilities in accordance with IAS 32. Where appropriate, currency and interest rate swaps have been presented alongside the underlying principal instrument. The carrying amounts of these instruments have been adjusted for the effect of the currency and interest rate swaps acting as hedges.

	2006		2005	
	Carrying value £m	Fair value £m	Carrying value £m	Fair value £m
At 31st December				
Liquid investments	1,035	1,035	1,025	1,025
Cash and cash equivalents	2,005	2,005	4,209	4,209
Current asset financial instruments	3,040	3,040	5,234	5,234
£ notes and bonds	(977)	(1,043)	(976)	(1,097)
US\$ notes, bonds and private financing	(1,435)	(1,446)	(1,929)	(1,932)
Notes and bonds swapped into US\$	(494)	(493)	(502)	(501)
Currency swaps	101	101	54	54
Interest rate swaps	(46)	(46)	(47)	(47)
	(1,874)	(1,884)	(2,424)	(2,426)
Notes swapped into Yen	(338)	(335)	(342)	(348)
Currency swaps	44	44	10	10
	(294)	(291)	(332)	(338)
€ notes	(1,671)	(1,620)	(1,702)	(1,705)
Interest rate swap	6	6	5	5
	(1,665)	(1,614)	(1,697)	(1,700)
Other short-term borrowings	(463)	(463)	(909)	(909)
Other long-term borrowings	(112)	(112)	(111)	(111)
Total borrowings and related swaps	(5,385)	(5,407)	(6,449)	(6,581)
Equity investments	441	441	362	362
Receivables	4,773	4,773	4,934	4,934
Payables	(4,581)	(4,581)	(4,754)	(4,754)
Other derivatives – assets	37	37	126	126
Other derivatives – liabilities	(49)	(49)	(150)	(150)
Other financial assets	263	263	271	271
Other financial liabilities	(232)	(232)	(391)	(391)
Net financial assets and liabilities	(1,693)	(1,715)	(817)	(949)
Total financial assets	8,710	8,710	10,996	10,996
Total financial liabilities	(10,403)	(10,425)	(11,813)	(11,945)
Reconciliation to net debt				
Liquid investments	1,035	1,035	1,025	1,025
Cash and cash equivalents	2,005	2,005	4,209	4,209
Total borrowings	(5,385)	(5,407)	(6,449)	(6,581)
	(2,345)	(2,367)	(1,215)	(1,347)
Less net effect of interest rate and currency swaps	(105)	(105)	(22)	(22)
Net debt	(2,450)	(2,472)	(1,237)	(1,369)

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39 Financial instruments and related disclosures continued

Interest rate profiles of financial assets and liabilities

The following tables set out the exposure of financial assets and liabilities to either fixed interest rates, floating interest rates or no interest rates. The maturity profile of financial assets and liabilities exposed to interest rate risk in the tables below indicates the contractual repricing and maturity dates of these instruments.

At 31st December 2006

Financial assets	Investments £m	Liquid investments £m	Cash and cash equivalents £m	Receivables £m	Other financial assets £m	Total £m
Less than one year	–	1,035	1,952	211	1	3,199
Between one and two years	–	–	–	3	–	3
Between two and three years	–	–	–	1	–	1
Between three and four years	–	–	–	–	–	–
Between four and five years	–	–	–	–	–	–
Greater than five years	–	–	–	–	104	104
Total interest earning	–	1,035	1,952	215	105	3,307
Analysed as:						
Fixed rate interest	–	285	12	207	104	608
Floating rate interest	–	750	1,940	8	1	2,699
Total interest earning	–	1,035	1,952	215	105	3,307
Non-interest earning	441	–	53	4,558	351	5,403
Total	441	1,035	2,005	4,773	456	8,710

At 31st December 2005

Financial assets	Investments £m	Liquid investments £m	Cash and cash equivalents £m	Receivables £m	Other financial assets £m	Total £m
Less than one year	–	1,025	4,188	204	94	5,511
Between one and two years	–	–	–	8	–	8
Between two and three years	–	–	–	13	–	13
Between three and four years	–	–	–	12	–	12
Between four and five years	–	–	–	–	–	–
Greater than five years	–	–	–	–	117	117
Total interest earning	–	1,025	4,188	237	211	5,661
Analysed as:						
Fixed rate interest	–	292	–	207	117	616
Floating rate interest	–	733	4,188	30	94	5,045
Total interest earning	–	1,025	4,188	237	211	5,661
Non-interest earning	362	–	21	4,697	255	5,335
Total	362	1,025	4,209	4,934	466	10,996

39 Financial instruments and related disclosures continued

At 31st December 2006		Effect of	Obligations		Other	
Financial liabilities	Debt	interest rate	under finance	Payables	financial	Total
	£m	swaps	leases	£m	liabilities	£m
		£m	£m		£m	
Less than one year	(895)	(1,883)	(106)	(14)	–	(2,898)
Between one and two years	(1,166)	1,164	(10)	–	–	(12)
Between two and three years	(339)	–	(7)	–	–	(346)
Between three and four years	(1)	–	(8)	–	–	(9)
Between four and five years	–	–	(6)	–	–	(6)
Greater than five years	(2,948)	719	(2)	–	–	(2,231)
Total interest bearing	(5,349)	–	(139)	(14)	–	(5,502)
Analysed as:						
Fixed rate interest	(4,721)	2,138	(46)	(6)	–	(2,635)
Floating rate interest	(628)	(2,138)	(93)	(8)	–	(2,867)
Total interest bearing	(5,349)	–	(139)	(14)	–	(5,502)
Non-interest bearing	(2)	–	–	(4,567)	(332)	(4,901)
Total	(5,351)	–	(139)	(4,581)	(332)	(10,403)

At 31st December 2005		Effect of	Obligations		Other	
Financial liabilities	Debt	interest rate	under finance	Payables	financial	Total
	£m	swaps	leases	£m	liabilities	£m
		£m	£m		£m	
Less than one year	(1,176)	(2,348)	(103)	(148)	(61)	(3,836)
Between one and two years	(287)	291	(3)	–	(23)	(22)
Between two and three years	(1,190)	1,185	(3)	–	–	(8)
Between three and four years	(343)	–	(2)	–	–	(345)
Between four and five years	–	–	(2)	–	–	(2)
Greater than five years	(3,354)	872	(8)	–	–	(2,490)
Total interest bearing	(6,350)	–	(121)	(148)	(84)	(6,703)
Analysed as:						
Fixed rate interest	(5,527)	2,348	(21)	–	(24)	(3,224)
Floating rate interest	(823)	(2,348)	(100)	(148)	(60)	(3,479)
Total interest bearing	(6,350)	–	(121)	(148)	(84)	(6,703)
Non-interest bearing	–	–	–	(4,606)	(504)	(5,110)
Total	(6,350)	–	(121)	(4,754)	(588)	(11,813)

Maturity analysis of interest earning financial assets

The maturity analysis of interest earning financial assets is equivalent to the maturity analysis presented in the interest rate profile table above.

Maturity analysis of interest bearing financial liabilities

At 31st December 2006		Debt	Finance	Payables	Total
Financial liabilities		£m	leases	£m	£m
			£m		
Within one year or on demand		(676)	(42)	(14)	(732)
Between one and two years		(1,166)	(36)	–	(1,202)
Between two and three years		(339)	(27)	–	(366)
Between three and four years		(11)	(15)	–	(26)
Between four and five years		–	(7)	–	(7)
After five years		(3,157)	(12)	–	(3,169)
		(5,349)	(139)	(14)	(5,502)

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39 Financial instruments and related disclosures continued

At 31st December 2005					
Financial liabilities	Debt £m	Finance leases £m	Payables £m	Other financial liabilities £m	Total £m
Within one year or on demand	(1,162)	(38)	(148)	(61)	(1,409)
Between one and two years	(287)	(30)	–	(23)	(340)
Between two and three years	(1,203)	(21)	–	–	(1,224)
Between three and four years	(343)	(11)	–	–	(354)
Between four and five years	(1)	(8)	–	–	(9)
After five years	(3,354)	(13)	–	–	(3,367)
	(6,350)	(121)	(148)	(84)	(6,703)

Currency profiles of financial assets and liabilities

The Group's currency exposures that give rise to net currency gains and losses that are recognised in the income statement arise principally in companies with Sterling functional currency. The tables below set out these exposures on financial assets and liabilities held in currencies other than the functional currencies of Group companies after the effect of currency swaps.

At 31st December 2006						
Financial assets	Sterling £m	US\$ £m	Euro £m	Yen £m	Other £m	Total £m
Investments	–	140	3	–	27	170
Cash and cash equivalents	2	81	6	2	18	109
Receivables	2	221	118	–	34	375
Other financial assets	–	2	1	–	4	7
	4	444	128	2	83	661

At 31st December 2005						
Financial assets	Sterling £m	US\$ £m	Euro £m	Yen £m	Other £m	Total £m
Investments	8	108	3	–	11	130
Cash and cash equivalents	1	46	10	2	19	78
Receivables	7	123	89	–	91	310
Other financial assets	–	–	–	–	–	–
	16	277	102	2	121	518

At 31st December 2006						
Financial liabilities	Sterling £m	US\$ £m	Euro £m	Yen £m	Other £m	Total £m
Debt	–	–	–	–	–	–
Obligations under finance leases	–	–	(9)	–	(8)	(17)
Payables	(14)	(117)	(67)	(2)	(93)	(293)
	(14)	(117)	(76)	(2)	(101)	(310)

At 31st December 2005						
Financial liabilities	Sterling £m	US\$ £m	Euro £m	Yen £m	Other £m	Total £m
Debt	–	–	(497)	–	–	(497)
Obligations under finance leases	–	(2)	–	–	–	(2)
Payables	(7)	(18)	(13)	(1)	(30)	(69)
	(7)	(20)	(510)	(1)	(30)	(568)

39 Financial instruments and related disclosures continued**Derivative financial instruments**

The table below sets out the net principal amount and fair value of derivative contracts held by GSK:

	Contract or underlying principal amount 2006 £m	Fair value	
		Assets 2006 £m	Liabilities 2006 £m
Currency and interest related instruments:			
Foreign exchange contracts	461	20	(25)
Cross currency swaps	838	150	(5)
Interest rate swaps	1,696	6	(46)
Equity related instruments:			
Options and warrants	407	13	(12)
Equity collar	270	–	(12)
Embedded derivatives	43	4	–
Total derivative financial instruments		193	(100)

	Contract or underlying principal amount 2005 £m	Fair value	
		Assets 2005 £m	Liabilities 2005 £m
Currency and interest related instruments:			
Foreign exchange contracts	(4,665)	102	(85)
Cross currency swaps	842	64	–
Interest rate swaps	1,848	5	(47)
Equity related instruments:			
Options and warrants	290	21	(49)
Equity collar	299	–	(14)
Embedded derivatives	34	3	(2)
Total derivative financial instruments		195	(197)

Derivative financial instruments

Included in 'Equity related instruments' above are variable sale forward contracts in Quest Diagnostics Inc. and options in Theravance Inc., as detailed below.

In 2002, GSK hedged part of the equity value of its holdings in Quest, its largest equity investment, through a series of variable sale forward contracts. The contracts ('the equity collar') were renewed in 2006 and are structured in five series, each over two million Quest shares, and mature between 2010 and 2012. The fair value of the contracts at 31st December 2006 was a liability of \$24 million (£12 million) (2005 – \$24 million (£14 million)). A second hedging contract over an additional 10 million shares was entered into on 15th February 2007 – see Note 38 'Post balance sheet events'.

The Group has entered into a put option agreement whereby Theravance's shareholders can sell up to half of their Theravance shares to GSK at a pre-determined price (\$19.375). Given the maximum number of shares subject to the put option, the Group's obligation is capped at \$525 million. At 31st December 2006, this option is recorded as a liability of \$19 million (£10 million) (2005 – \$81 million (£47 million)). As at 31st December 2006, the maximum potential exposure to GSK from fair value movements of these options is therefore approximately \$506 million (£258 million) (2005 – \$444 million (£258 million)). The expiry date is August 2007.

The Group has entered into a call option agreement whereby it can purchase half of the outstanding Theravance shares in issue at a pre-determined price (\$54.25). At 31st December 2006, this option is recorded as an asset of \$15 million (£8 million) (2005 – \$28 million (£16 million)). As at 31st December 2006, the maximum potential exposure to GSK from fair value movements of this option is therefore \$15 million. The expiry date is July 2007.

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39 Financial instruments and related disclosures continued

The following table sets out the principal amount and fair values of derivative contracts which qualify for hedge accounting treatment:

	2006		2005	
	Contract or underlying principal amount £m	Fair value of derivative contract £m	Contract or underlying principal amount £m	Fair value of derivative contract £m
Cash flow hedges:				
Cross currency swaps	338	44	342	10
Fair value hedges:				
Foreign exchange contracts	–	–	2,151	74
Interest rate swaps	1,696	(40)	1,848	(42)
Cross currency swaps	500	(5)	500	3
Net investment hedges:				
Foreign exchange contracts	(5,049)	11	(6,816)	(57)
Cross currency swaps	500	106	500	51

Cash flow hedges

The Group has entered into a cross currency swap and designated it a cash flow hedge converting fixed Euro coupons, payable annually, to fixed Yen payments. The bond matures in 2009. The risk being hedged is the variability of cash flows arising from currency fluctuations.

Fair value hedges

The Group has designated interest rate swaps and the interest element of cross currency swaps as fair value hedges. The risk being hedged is the variability of the fair value of the bonds arising from interest rate fluctuations.

Net investment hedges

Foreign exchange contracts and the currency element of cross currency swaps have been designated as net investment hedges in respect of the foreign currency translation risk arising on consolidation of the Group's net investment in its US dollar, Euro and Yen foreign operations.

40 Employee share schemes

The Group operates share option schemes, whereby options are granted to employees to acquire shares or ADSs in GlaxoSmithKline plc at the grant price, savings-related share option schemes and share award schemes, whereby awards are granted to employees to acquire shares or ADSs in GlaxoSmithKline plc at no cost, subject to the achievement by the Group of specified performance targets. In 2004, the Group introduced a new share award scheme, the Share Value Plan, whereby awards are granted to employees to acquire shares or ADSs in GlaxoSmithKline plc at no cost after a three year vesting period. The granting of restricted share awards has replaced the granting of options to certain employees as the cost of the scheme more readily equates to the potential gain to be made by the employee.

Grants under share option schemes are normally exercisable between three and ten years from the date of grant. Grants of restricted shares and share awards are normally exercisable at the end of the three year vesting/performance period. Grants under savings-related share option schemes are normally exercisable after three years' saving. Options under the share option schemes are granted at the market price ruling at the date of grant. In accordance with UK practice, the majority of options under the savings-related share option schemes are granted at a price 20% below the market price ruling at the date of grant.

Share options awarded to the Directors and, with effect from the 2004 grant, the CET are subject to performance criteria as laid out in the Remuneration Report.

The stock-based compensation charge has been recorded in the income statement as follows:

	2006 £m	2005 £m	2004 £m
Cost of sales	18	17	35
Selling, general and administration	143	150	207
Research and development	65	69	91
	226	236	333

40 Employee share schemes continued**Option pricing**

For the purposes of valuing options to arrive at the stock-based compensation charge, the Black-Scholes option pricing model has been used. The assumptions used in the model for 2004, 2005 and 2006 are as follows:

	2006	2005	2004
Risk-free interest rate	4.2% – 5.0%	4.0% – 4.8%	3.3% – 4.6%
Dividend yield	3.3%	3.0%	3.2%
Volatility	18% – 29%	21% – 28%	26% – 29%
Expected lives of options granted under:			
Share option schemes	5 years	5 years	5 years
Savings-related share option schemes	3 years	3 years	3 years
Weighted average share price for grants in the year:			
Ordinary shares	£14.64	£13.15	£11.25
ADSs	\$51.40	\$47.42	\$43.23

Volatility was determined based on the three year share price history. The fair value of performance share plan grants take into account market conditions. Expected lives of options were determined based on weighted average historic exercises of options.

Options outstanding

	Share option schemes – shares			Share option schemes – ADSs			Savings-related share option schemes		
	Number 000	Weighted exercise price	Weighted fair value	Number 000	Weighted exercise price	Weighted fair value	Number 000	Weighted exercise price	Weighted fair value
At 1st January 2004	205,705	£14.89		106,529	\$46.58		10,583	£9.59	
Options granted	9,837	£11.23	£2.49	9,222	\$42.99	\$8.54	1,580	£9.52	£3.30
Options exercised	(5,764)	£6.54		(1,845)	\$25.65		(232)	£9.18	
Options lapsed	(11,997)	£15.33		(3,427)	\$48.28		(1,790)	£10.46	
At 31st December 2004	197,781	£14.92		110,479	\$46.57		10,141	£9.44	
Options granted	516	£12.57	£2.76	956	\$45.66	\$9.90	5,167	£11.45	£3.68
Options exercised	(10,483)	£9.91		(7,537)	\$38.83		(5,732)	£9.16	
Options lapsed	(20,888)	£17.16		(8,306)	\$50.26		(810)	£11.02	
At 31st December 2005	166,926	£14.97		95,592	\$46.86		8,766	£10.66	
Options granted	9,776	£14.78	£3.53	7,940	\$51.36	\$11.59	2,069	£11.40	£3.41
Options exercised	(13,244)	£11.66		(13,310)	\$41.78		(2,009)	£9.48	
Options lapsed	(6,755)	£15.35		(1,791)	\$46.88		(653)	£10.97	
At 31st December 2006	156,703	£15.22		88,431	\$48.02		8,173	£11.11	
Range of exercise prices	£10.06 – £19.77			\$32.09 – \$61.35			£10.20 – £11.45		
Weighted average remaining contractual life		4.9 years			5.6 years			2.4 years	

The total intrinsic value (the amount by which the share price exceeded the exercise price of the option) of options exercised during 2006 was £129 million (2005 – £122 million).

The aggregate intrinsic value of options outstanding at 31st December 2006 was £342 million.

Notes to the financial statements

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40 Employee share schemes continued

In order to encourage employees to convert options, excluding savings-related share options, held over Glaxo Wellcome or SmithKline Beecham shares or ADSs, into those over GlaxoSmithKline shares or ADSs, a programme was established to give an additional cash benefit of 10% of the exercise price of the original option provided that the employee did not voluntarily leave the Group for two years from the date of the merger and did not exercise the option before the earlier of six months from the expiry date of the original option and two years from the date of the merger. The cash benefit will also be paid if the options expire unexercised if the market price is below the exercise price on the date of expiry.

Options outstanding at 31st December 2006

Year of grant	Share option schemes – shares			Share option schemes – ADSs			Savings-related share option schemes		
	Number 000	Weighted exercise price	Latest exercise date	Number 000	Weighted exercise price	Latest exercise date	Number 000	Exercise price	Latest exercise date
1997	4,379	£11.85	13.11.07	2,130	\$40.20	13.11.07	–	–	–
1998	14,286	£16.91	23.11.08	5,132	\$54.29	23.11.08	–	–	–
1999	15,225	£18.20	01.12.09	6,966	\$60.15	24.11.09	–	–	–
2000	14,649	£14.90	11.09.10	326	\$58.88	09.08.10	–	–	–
2001	42,824	£18.12	29.11.11	27,450	\$51.84	28.11.11	–	–	–
2002	19,302	£11.95	03.12.12	9,838	\$37.60	03.12.12	–	–	–
2003	27,318	£12.67	14.12.13	19,396	\$43.55	14.12.13	179	£10.20	31.05.07
2004	8,922	£11.23	02.12.14	8,919	\$43.05	02.12.14	1,268	£9.52	31.05.08
2005	206	£13.08	01.11.15	464	\$47.33	31.10.15	4,663	£11.45	31.05.09
2006	9,592	£14.69	28.11.16	7,810	\$51.34	28.07.16	2,063	£11.40	31.05.10
Total	156,703	£15.22		88,431	\$48.02		8,173	£11.11	

All of the above options are exercisable, except all options over shares and ADSs granted in 2004, 2005 and 2006 and the savings-related share options granted in 2004, 2005 and 2006. The total number of non-vested options at 31st December 2006 was 26,713,865 share options and 17,192,398 ADS options (2005 – 45,645,311 share options and 31,326,848 ADS options). These options had a weighted average grant date fair value of £3.53 for share options, \$11.59 for ADS options and £3.41 for savings-related share options (2005 – £2.95, \$2.72 and £3.68 respectively).

There has been no change in the effective exercise price of any outstanding options during the year.

Options exercisable

	Share option schemes – shares			Share option schemes – ADSs			Savings-related share option schemes		
	Number 000	Weighted exercise price	Weighted fair value	Number 000	Weighted exercise price	Weighted fair value	Number 000	Weighted exercise price	Weighted fair value
At 31st December 2004	126,917	£16.49		57,421	\$51.75		270	£14.12	
At 31st December 2005	128,316	£15.77		64,265	\$48.56		1,429	£9.16	
At 31st December 2006	137,983	£15.51		71,238	\$48.32		179	£10.20	
Weighted average remaining contractual life		4.4 years			4.9 years			0.3 years	
Options vested during the year	24,991		£3.27	18,103		\$12.35	789		£4.15

The aggregate intrinsic value of options exercisable at 31st December 2006 was £251 million. The total fair value of options vesting during the year was £206 million (2005 – £250 million; 2004 – £630 million).

40 Employee share schemes continued**GlaxoSmithKline share award schemes****Performance Share Plan**

The Group operates a Performance Share Plan whereby awards are granted to Directors and senior executives at no cost. The percentage of each award that vests is based upon the performance of the Group over a three year measurement period. The performance conditions consist of two parts, each of which applies to 50% of the award. For awards granted in 2003, the first part of the condition compares GlaxoSmithKline's Total Shareholder Return (TSR) over the period with the TSR of companies in the UK FTSE 100 Index over the same period. For awards granted in 2004, and subsequent years, the first part of the condition compares GlaxoSmithKline's TSR over the period with the TSR of 13 pharmaceutical companies in the comparator group over the same period. The second part of the performance condition compares GlaxoSmithKline's earnings per share growth to the increase in the UK Retail Prices Index over the three year performance period. Awards granted to Directors and members of the CET from 15th December 2003 are subject to a single performance condition which compares GlaxoSmithKline's TSR over the period with the TSR of companies in the comparator group over the same period.

Number of shares and ADSs issuable	Shares Number (000)	Weighted fair value	ADSs Number (000)	Weighted fair value
At 1st January 2004	3,500		2,479	
Awards granted	1,778	£7.25	1,339	\$23.89
Awards exercised	(409)		(187)	
Awards cancelled	(520)		(276)	
At 31st December 2004	4,349		3,355	
Awards granted	130	£9.02	88	\$32.34
Awards exercised	(375)		(199)	
Awards cancelled	(477)		(237)	
At 31st December 2005	3,627		3,007	
Awards granted	2,068	£10.06	1,452	\$35.13
Awards exercised	(438)		(187)	
Awards cancelled	(501)		(238)	
At 31st December 2006	4,756		4,034	

Share Value Plan

The Group operates a Share Value Plan whereby awards are granted, in the form of shares, to certain employees at no cost. The awards vest after three years. There are no performance criteria attached.

Number of shares and ADSs issuable	Shares Number (000)	Weighted fair value	ADSs Number (000)	Weighted fair value
At 1st January 2004	–		–	
Awards granted	4,419	£10.07	3,562	\$38.14
At 31st December 2004	4,419		3,562	
Awards granted	403	£12.00	511	\$44.39
Awards exercised	(138)		(143)	
Awards cancelled	(170)		(81)	
At 31st December 2005	4,514		3,849	
Awards granted	4,759	£13.45	4,126	\$52.53
Awards exercised	(131)		(66)	
Awards cancelled	(348)		(280)	
At 31st December 2006	8,794		7,629	

Notes to the financial statements

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40 Employee share schemes continued

Employee Share Ownership Plan Trusts

The Group sponsors Employee Share Ownership Plan (ESOP) Trusts to acquire and hold shares in GlaxoSmithKline plc to satisfy awards made under employee incentive plans and options granted under employee share option schemes. The trustees of the ESOP Trusts purchase shares on the open market with finance provided by the Group by way of loans or contributions. Costs of running the ESOP Trusts are charged to the income statement. Shares held by the ESOP Trusts are deducted from other reserves and held at the value of proceeds receivable from employees on exercise. If there is deemed to be a permanent diminution in value this is reflected by a transfer to retained earnings. The Trusts also acquire and hold shares to meet notional dividends re-invested on deferred awards under the SmithKline Beecham Mid-Term Incentive Plan. The trustees have waived their rights to dividends on the shares held by the ESOP Trusts.

Shares held for share award schemes	2006	2005
Number of shares ('000)	37,508	22,169
	£m	£m
Nominal value	9	6
Carrying value	196	116
Market value	504	326
Shares held for share option schemes	2006	2005
Number of shares ('000)	115,943	145,267
	£m	£m
Nominal value	29	36
Carrying value	1,803	2,197
Market value	1,558	2,134

41 Reconciliation to US accounting principles

The analyses and reconciliations presented in this Note represent the financial information prepared on the basis of US Generally Accepted Accounting Principles (US GAAP) rather than IFRS.

Summary of material differences between IFRS and US GAAP

Acquisition of SmithKline Beecham

The Group has exercised the exemption available under IFRS 1 'First-time Adoption of IFRS' not to restate business combinations prior to the date of transition of the Group's reporting GAAP from UK Generally Accepted Accounting Principles (UK GAAP) to IFRS. Therefore the combination in 2000 of Glaxo Wellcome plc and SmithKline Beecham plc continues to be accounted for as a merger (pooling of interests) in accordance with UK GAAP at that time. Under US GAAP, this business combination did not qualify for pooling of interests accounting and Glaxo Wellcome was deemed to be the accounting acquirer in a purchase business combination.

Accordingly the net assets of SmithKline Beecham were recognised at fair value as at the date of acquisition. As a result of the fair value exercise, increases in the values of SmithKline Beecham's inventory, property, plant and equipment, intangible assets, investments and pension obligations were recognised and fair market values attributed to its internally-generated intangible assets, mainly product rights (inclusive of patents and trademarks) and in-process research and development, together with appropriate deferred taxation effects. The difference between the cost of acquisition and the fair value of the assets and liabilities of SmithKline Beecham is recorded as goodwill.

Capitalised interest

Under IFRS, the Group does not capitalise interest. US GAAP requires interest incurred as part of the cost of constructing a fixed asset to be capitalised and amortised over the life of the asset.

Goodwill

The Group has exercised the exemption available under IFRS 1 not to restate business combinations prior to the date of transition of the Group's reporting GAAP from UK GAAP to IFRS. Under UK GAAP, goodwill arising on acquisitions before 1998 accounted for under the purchase method was eliminated against equity, and under IFRS, on future disposal or closure of a business, any goodwill previously taken directly to equity under a former GAAP will not be charged against income. Under UK GAAP, goodwill arising on acquisitions from 1998 was capitalised and amortised over a period not exceeding 20 years. On the date of the Group's transition to IFRS, 1st January 2003, amortisation ceased in accordance with IFRS 3 'Business combinations'. The Group must instead identify and value its reporting units for the purpose of assessing, at least annually, potential impairment of goodwill allocated to each reporting unit. As permitted by the business combinations exemption available under IFRS 1, amortisation arising prior to 2003 was not reversed.

Under US GAAP, goodwill arising on acquisitions prior to 30th June 2001 was capitalised and amortised over a period not exceeding 40 years. In July 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard (SFAS) 142, 'Goodwill and Other Intangible Assets'. Like IFRS 3, SFAS 142 requires that goodwill must not be amortised and that annual impairment tests of goodwill must be undertaken. The implementation of SFAS 142 in 2002, a year earlier than the Group's transition to IFRS, results in goodwill balances acquired between 1998 and 2003 reflecting one year less of amortisation under US GAAP than under IFRS.

Under IFRS, costs to be incurred in integrating and restructuring the Wellcome, SmithKline Beecham and Block Drug businesses following the acquisitions in 1995, 2000 and 2001 respectively were charged to the income statement post acquisition. Similarly, integration and restructuring costs arising in respect of the acquisitions of CNS in 2006 and Corixa and ID Biomedical in 2005 have been charged to the income statement under IFRS. Under US GAAP, certain of these costs are considered in the allocation of purchase consideration thereby affecting the goodwill arising on acquisition.

In-process research & development (IPR&D)

Under IFRS, IPR&D projects acquired in a business combination are capitalised and remain on the balance sheet, subject to any impairment write-downs. Amortisation is charged over the assets' estimated useful lives from the point when the assets become available for use. Under US GAAP, such assets are recognised in the opening balance sheet but are then written off immediately to the income statement, as the technological feasibility of the IPR&D has not yet been established and it has no alternative future use. Under IFRS, deferred tax is provided for IPR&D assets acquired in a business combination. US GAAP does not provide for deferred tax on these assets, resulting in a reconciling adjustment to deferred tax and goodwill.

IPR&D acquired in transactions other than business combinations is discussed under Intangible assets below.

Intangible assets

Under IFRS, certain intangible assets related to specific compounds or products which are purchased from a third party and are developed for commercial applications are capitalised but not subject to amortisation until regulatory approval is obtained. Under US GAAP, payments made in respect of these compounds or products which are still in development and have not yet received regulatory approval are charged directly to the income statement.

Under IFRS, intangible assets are amortised over their estimated useful economic life except in the case of certain acquired brands where the end of the useful economic life of the brand cannot be foreseen. Under US GAAP, until the implementation of SFAS 142 'Goodwill and Other Intangible Assets' in 2002, all intangible assets, including brands, were amortised over a finite life. On implementation of SFAS 142 in 2002, intangible assets deemed to have indefinite lives were no longer amortised. As a result of the difference in accounting treatment prior to the implementation of SFAS 142, the carrying values of indefinite lived brands are affected by amortisation charged before 2002 under US GAAP.

Notes to the financial statements

continued

41 Reconciliation to US accounting principles continued

Restructuring costs

Under IFRS, restructuring costs incurred following acquisitions are charged to the profit and loss account post acquisition. For US GAAP purposes, certain of these costs are recognised as liabilities upon acquisition in the opening balance sheet.

Other restructuring costs are recorded as a provision under IFRS when a restructuring plan has been announced. Under US GAAP, a provision may only be recognised when further criteria are met or the liability is incurred. Therefore adjustments have been made to eliminate provisions for restructuring costs that do not meet US GAAP requirements.

Marketable securities

Marketable securities consist primarily of equity securities and certain other liquid investments, principally government bonds and short-term corporate debt instruments. Under SFAS 115 'Accounting for Certain Investments in Debt and Equity Securities', these securities are considered available for sale and are carried at fair value, with the unrealised gains and losses, net of tax, recorded as a separate component of shareholders' equity. Under IFRS, these are accounted for as available-for-sale financial assets in accordance with IAS 39 'Financial Instruments : Recognition and Measurement'.

The accounting treatment for marketable securities under US GAAP and IFRS is similar. However, differences do arise, principally as a result of the category of marketable securities as defined by SFAS 115 being smaller than the category of available-for-sale financial assets as defined by IAS 39. Investments which are not marketable securities under the SFAS 115 definition are accounted for at cost less impairments under US GAAP rather than at fair value.

The Group did not adopt IAS 39 until 1st January 2005, and, in accordance with the exemption available under IFRS 1, has presented financial instruments in the comparative periods in accordance with UK GAAP. Therefore in 2004 these securities are stated at the lower of cost and net realisable value.

Marketable securities are reviewed at least every quarter for other than temporary impairment. For equity securities, the factors considered include:

- the investee's current financial performance and future prospects
- the general market condition of the geographic or industry area in which the investee operates
- the duration and extent to which the market value has been below cost.

Gross unrealised gains and losses on marketable securities were £142 million and less than £1 million, respectively, at 31st December 2006 (2005 – £36 million and £4 million, respectively). The fair value of marketable securities with unrealised losses at 31st December 2006 is £3 million (2005 – £62 million). All of these marketable securities have been in a continuous loss position for less than 12 months. Deferred tax provided against unrealised gains and losses at 31st December 2006 was £21 million (2005 – £4 million). Gains of £8 million were reclassified out of accumulated other comprehensive income into the income statement on disposals of equity investments during the year (2005 – £7 million gain).

The proceeds from sale of marketable securities under US GAAP were £19,013 million in the year ended 31st December 2006 (2005 – £19,416 million). The proceeds include the roll-over of liquid funds on short-term deposit. The gross gains and losses reflected in the consolidated income statement in respect of marketable securities were £11 million and £nil, respectively (2005 – £7 million and £nil).

Pensions and other post-retirement benefits

The key difference between IFRS and US GAAP is the method of recognition of actuarial gains and losses. GSK has opted under IFRS to recognise actuarial gains and losses in the statement of recognised income and expense in the year in which they arise. Under US GAAP actuarial gains and losses are recognised using the 10% corridor approach and deferred actuarial gains and losses are amortised.

Stock-based compensation

Under IFRS 2 'Share-based Payment', share options are fair valued at their grant dates and the cost is charged to the income statement over the relevant vesting periods. Under US GAAP, the Group applies SFAS 123R 'Share-Based Payment' and related accounting interpretations in accounting for its option plans, which also require options to be fair valued at their grant date and charged to the income statement over the vesting period of the options. Minor differences arise as a result of the differing definitions of grant date for certain share-based payments and in the accounting treatment of share options with certain conditions linked to inflation, which are classified as liabilities under SFAS 123R.

Derivative instruments

SFAS 133, 'Accounting for Derivative Instruments and Hedging Activities', as amended by SFAS 137 and SFAS 138 and as interpreted by the Derivatives Implementation Group, was adopted by the Group with effect from 1st January 2001. SFAS 133 establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts (collectively, referred to as derivatives) and for hedging activities. SFAS 133 requires that an entity recognise all derivatives as either assets or liabilities in the consolidated balance sheet and measure those instruments at fair value. Changes in fair value over the period are recorded in current earnings unless hedge accounting is obtained. SFAS 133 prescribes requirements for designation and documentation of hedging relationships and ongoing assessments of effectiveness in order to qualify for hedge accounting.

The Group also evaluates contracts for 'embedded' derivatives. In accordance with SFAS 133 requirements, if embedded derivatives are not clearly and closely related to the host contract, they are accounted for separately from the host contract as derivatives.

The key differences between IFRS under which the Group's financial statements are prepared and US GAAP, and in the Group's application of their respective requirements, are:

- certain derivatives which are designated by the Group as hedging instruments under IAS 39 are not designated as hedging instruments under SFAS 133. Accordingly, hedge accounting is not applied under US GAAP in respect of these arrangements

41 Reconciliation to US accounting principles

continued

- the definition of derivatives within the scope of SFAS 133 excludes instruments for which there is no liquid market. This leads to certain items not being recognised on the balance sheet, although they are accounted for as derivatives under IFRS, most notably the call option over Theravance shares
- IAS 39 has an exemption from the requirement to recognise embedded foreign currency derivatives where the currency is commonly used in the economic environment of the host contract. SFAS 133 does not grant a similar exemption and so the Group identifies and separately accounts for more embedded derivatives under US GAAP than it does under IFRS.

In 2005 the Group exercised the exemption available under IFRS 1 to present financial instruments in the comparative periods in accordance with UK GAAP. Under UK GAAP, some derivative instruments used for hedges were not recognised on the balance sheet and the matching principle was used to match the gain or loss under these hedging contracts to the foreign currency transaction or profits to which they related. Gains and losses related to the fair value adjustments on these derivative instruments are therefore reconciling items in the 2004 comparative period presented in the reconciliation of profit. In 2006 and 2005, the Group did not designate any of its derivatives as qualifying hedge instruments under SFAS 133.

Hedging arrangements under US GAAP

As at 31st December 2006, the Group applied \$500 million of borrowings (2005 – \$1 billion) to hedge the foreign currency exposures of the Group's net investment in certain foreign operations. These borrowings are designated as hedges of net investments. The effective portion of foreign exchange gains or losses on these hedges is recorded as part of the foreign currency translation component of other comprehensive income. In 2006, £32 million of after tax gains (2005 – £42 million of after tax losses) were recorded in other comprehensive income.

Valuation of derivative instruments

The fair value of derivative instruments is sensitive to movements in the underlying market rates and variables. The Group monitors the fair value of derivative instruments on at least a quarterly basis. Derivatives, including interest rate swaps and cross-currency swaps, are valued using standard valuation models, counterparty valuations, or third party valuations. Standard valuation models used by the Group consider relevant discount rates, the market yield curve on the valuation date, forward currency exchange rates and counterparty risk. All significant rates and variables are obtained from market sources. All valuations are based on the remaining term to maturity of the instrument.

Foreign exchange contracts are valued using forward rates observed from quoted prices in the relevant markets when possible. The Group assumes parties to long-term contracts are economically viable but reserves the right to exercise early termination rights if economically beneficial when such rights exist in the contract.

Dividends

Under IFRS, GSK plc's quarterly dividends are recognised only on payment. Under US GAAP, the dividends are recognised in the financial statements when they are declared.

Other

The following adjustments are also included in the reconciliations:

- computer software – under IFRS, the Group capitalises costs incurred in acquiring and developing computer software for internal use where the software supports a significant business system and the expenditure leads to the creation of a durable asset. For US GAAP, the Group applies SOP 98-1, 'Accounting for the Costs of Computer Software Developed or Obtained for Internal Use', which restricts the categories of costs which can be capitalised
- variable interest entities – under the FASB's Interpretation No. 46 Revised (FIN 46R), 'Consolidation of Variable Interest Entities', certain entities, known as Variable Interest Entities (VIEs), must be consolidated by the 'primary beneficiary' of the entity. The primary beneficiary is generally defined as having the majority of the risks and rewards arising from the VIE. Additionally, for VIEs in which a significant, but not majority, variable interest is held, certain disclosures are required. The Group regularly reviews potential VIEs and, as a consequence, consolidated Theravance Inc. between May 2004 and February 2006 (see Note (c) on page 147). No other VIEs of which the Group is the primary beneficiary have been identified
- fixed asset and inventory impairments – reversals of impairments previously recorded against the carrying value of assets are permitted under IFRS in certain circumstances. US GAAP does not permit reversals of these impairments
- various other small adjustments.

Consolidated summary statement of cash flows

The US GAAP cash flow statement reports three categories of cash flows: operating activities (including tax and interest); investing activities (including capital expenditure, acquisitions and disposals together with cash flows from available-for-sale current asset investments); and financing activities (including dividends paid). A summary statement of cash flows is presented on page 144.

Comprehensive income statement

The requirement of SFAS 130, 'Reporting comprehensive income', to provide a comprehensive income statement is met under IFRS by the Statement of recognised income and expense (page 89).

Recent pronouncements**Share-based payment**

On 1st January 2006, the Group adopted SFAS 123R, 'Share-Based Payment' using the modified prospective application method. Prior to this, GSK applied the fair value provisions of SFAS 123, 'Accounting for Stock-Based Compensation' in accounting for employee share-based compensation awards. The adoption of SFAS 123R had the following impact on the Group's consolidated financial statements:

- Under SFAS 123, the Group had elected to account for the forfeiture of non-vested stock options as incurred. As a result of adopting SFAS 123R, the Group is now required to estimate total forfeitures at the grant date, and revise its estimate throughout the vesting period. The impact of estimating the level of option forfeitures in advance of actual occurrence reduces the cumulative compensation cost recognised in respect of options outstanding at the date of adoption of SFAS 123R of 1st January 2006 by £19 million (£12 million net of tax). This has been recognised as a cumulative effect of a change in accounting principle

41 Reconciliation to US accounting principles

continued

- Under SFAS 123R share options whose vesting is indexed to a factor that is not a market, performance or service condition are classified as liabilities on the balance sheet and remeasured to fair value at each reporting date. Accordingly, share options granted by GSK with a condition linked to inflation are accounted for as liabilities under US GAAP. Under IFRS, these options are accounted for as equity-settled share-based payments, so their fair value is measured at grant date only and this is recognised over the vesting period in shareholders' funds. The impact of accounting for options outstanding at 1st January 2006 on the revised US GAAP basis increases the cumulative compensation cost recognised by £3 million (£2 million net of tax). This has been recognised as a cumulative effect of a change in accounting principle
- Under SFAS 123, the Group allocated share option compensation expense based on the nominal vesting period, rather than the expected time to achieve retirement eligibility. SFAS 123R specifies that a share-based award is considered vested for expense attribution purposes when the employee's retention of the award is no longer contingent upon providing subsequent service. Accordingly, the Group has prospectively revised its expense attribution method so that the related compensation cost is recognised over the period from the grant date to the date retirement eligibility is achieved, if less than the stated vesting period. The impact of this change was not significant.

For the year ended 31st December 2006, compensation expense for all types of share-based payment arrangements and the related income tax benefit recognised was £252 million and £26 million, respectively. Had the Group continued to account for compensation expense under the fair value provisions of SFAS 123, the compensation expense would not have been materially different from the SFAS 123R expense for the year.

At 31st December 2006, GSK had approximately £288 million of total unrecognised compensation cost related to non-vested share-based compensation arrangements granted under the plans, of which £135 million relates to share option schemes. The total cost is expected to be recognised over a weighted-average period of 1.9 years, and 1.8 years for share option schemes.

The tax benefit realised from share options exercised during 2006 was £54 million.

Pensions and other post retirement benefits

In September 2006, the FASB issued SFAS 158, 'Employers' Accounting for Defined Benefit Pension and Other Post-retirement Plans'. SFAS 158 requires GSK to (i) recognise the overfunded or underfunded status of a defined benefit plan (other than a multi-employer plan) as an asset or liability with changes in that funded status recognised through comprehensive income; (ii) measure the funded status of a plan as of the year-end date; and (iii) provide additional disclosures.

The Group adopted SFAS 158 in 2006 and has initially recognised the funded status of the defined benefit post-retirement plan and provided the required disclosures at 31st December 2006. Retrospective application was not permitted, therefore in 2005 and 2004 actuarial gains and losses were recognised using the 10% corridor approach and deferred actuarial gains and losses were amortised.

The impact of the adoption of SFAS 158 on the Group's consolidated financial statements is disclosed in note (f) within this Note.

Accounting for uncertain tax positions

In July 2006, the FASB issued FIN 48, 'Accounting for Uncertain Tax Positions'. FIN 48 clarifies the accounting for uncertainty in income taxes recognised in an enterprise's financial statements under US GAAP, in accordance with SFAS 109, 'Accounting for Income Taxes'. The interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, disclosure and transition. The Group is currently evaluating the potential impacts of FIN 48 on its US GAAP financial statements. For the Group, the interpretation will be effective from 1st January 2007.

Other Pronouncements

- SFAS 157 – In September 2006, the FASB issued SFAS 157, 'Fair Value Measurements'. This Statement defines fair value, establishes a framework for measuring fair value in US GAAP, and expands disclosures about fair value measurements. The Statement refers to other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. This Statement does not require any new fair value measurements. For the Group, the Statement will be effective on 1st January 2008
- SFAS 159 – In February 2007, the FASB issued SFAS 159, 'The Fair Value Option for Financial Assets and Financial Liabilities'. This Statement permits entities to choose to elect, at specified election dates, to measure eligible financial instruments at fair value. Unrealised gains and losses on items for which the fair value option has been elected would be reported in net income at each subsequent reporting date, and upfront costs and fees related to those items would be recognised in net income as incurred and not deferred. The Group is unlikely to elect to exercise the Fair Value Option
- SAB 108 – In September 2006, the SEC staff issued Staff Accounting Bulletin No. 108. SAB 108 establishes a dual approach for qualifying financial statement errors, requiring evaluation of errors under both the iron curtain and the roll-over methods. The guidance applies to the Group's US GAAP financial information for 2006 and accordingly has been adopted by the Group. SAB 108 has had no impact on the US GAAP financial information presented in this Note.

41 Reconciliation to US accounting principles continued

The following is a summary of the material adjustments to profit and shareholders' funds which would be required if US GAAP had been applied instead of IFRS.

Profit	Notes	2006 £m	2005 £m	2004 £m
Profit after taxation for the year under IFRS		5,498	4,816	4,022
Profit attributable to minority interests		(109)	(127)	(114)
Profit attributable to shareholders under IFRS		5,389	4,689	3,908
US GAAP adjustments:				
Goodwill impairment		10	–	–
Amortisation and impairment of intangible assets	b	(1,276)	(1,584)	(1,441)
Acquisition and disposal of product rights	b	(111)	(72)	(210)
Write-off of in-process R&D acquired in business combinations	b	(14)	(26)	–
Depreciation and impairment of other assets		(93)	(40)	(2)
Capitalised interest		4	(1)	(17)
Disposal of interests in associates and subsidiaries		–	–	(97)
Investments		(10)	(2)	(30)
Pensions and post-retirement benefits	f	(171)	(127)	(126)
Stock-based compensation		(26)	6	13
Derivative instruments and hedging		477	(30)	33
Fair value of put option granted to minority shareholders	c	–	–	17
Restructuring costs		(16)	1	(12)
Tax benefits on exercise of stock options	d	16	(47)	(10)
Deferred taxation	d	276	585	757
Other		–	(16)	(51)
Net income under US GAAP before cumulative effect of change in accounting principle		4,455	3,336	2,732
Cumulative effect of change in accounting principle		10	–	–
Net income under US GAAP		4,465	3,336	2,732
Earnings per share under US GAAP		2006 p	2005 p	2004 p
Basic net income per share before cumulative effect of change in accounting principle		78.9	58.8	47.6
Cumulative effect of change in accounting principle per share		0.2	–	–
Basic net income per share after cumulative effect of change in accounting principle		79.1	58.8	47.6
Diluted net income per share before cumulative effect of change in accounting principle		78.2	58.3	47.5
Cumulative effect of change in accounting principle per share		0.2	–	–
Diluted net income per share after cumulative effect of change in accounting principle		78.4	58.3	47.5
Earnings per ADS under US GAAP		2006 \$	2005 \$	2004 \$
Basic net income per ADS before cumulative effect of change in accounting principle		2.92	2.14	1.74
Cumulative effect of change in accounting principle per ADS		0.01	–	–
Basic net income per ADS after cumulative effect of change in accounting principle		2.93	2.14	1.74
Diluted net income per ADS before cumulative effect of change in accounting principle		2.89	2.12	1.74
Cumulative effect of change in accounting principle per ADS		0.01	–	–
Diluted net income per ADS after cumulative effect of change in accounting principle		2.90	2.12	1.74

Notes to the financial statements

continued

41 Reconciliation to US accounting principles continued

Equity shareholders' funds	Notes	2006 £m	2005 £m
Total equity under IFRS		9,648	7,570
Minority interests		(262)	(259)
Shareholders' equity under IFRS		9,386	7,311
US GAAP adjustments:			
Goodwill	a	17,949	17,976
Product rights	b	10,634	12,065
Pension intangible asset	f	–	86
Fixed assets		(35)	33
Inventory impairment reversals		(54)	(30)
Capitalised interest		183	179
Investments		500	576
Pensions and other post-retirement benefits	f	35	1,163
Restructuring costs		39	65
Derivative instruments		(44)	(33)
Dividends		(676)	(568)
Deferred taxation	e	(3,262)	(4,531)
Other		(2)	(10)
Shareholders' equity under US GAAP		34,653	34,282

Consolidated statement of cash flows under US GAAP	2006 £m	2005 £m	2004 £m
Net cash provided by operating activities	4,163	5,751	4,618
Net cash used in investing activities	(1,752)	(1,843)	(988)
Net cash used in financing activities	(4,345)	(2,409)	(3,038)
Net increase in cash and cash equivalents	(1,934)	1,499	592
Exchange rate movements	(282)	237	(93)
Cash and cash equivalents at beginning of year	4,221	2,485	1,986
Cash and cash equivalents at end of year	2,005	4,221	2,485

41 Reconciliation to US accounting principles continued

Notes to the Profit and Equity shareholders' funds reconciliations

(a) Goodwill

The following tables set out the IFRS to US GAAP adjustments required to the IFRS balance sheet in respect of goodwill.

Balance sheet	2006 £m	2005 £m
Goodwill under IFRS	758	696
Goodwill under US GAAP	18,707	18,672
IFRS to US GAAP adjustments	17,949	17,976

Of the £18,707 million US GAAP goodwill balance at 31st December 2006 (2005 – £18,672 million), £15,875 million (2005 – £15,875 million) is in respect of the goodwill arising on the acquisition of SmithKline Beecham by Glaxo Wellcome in 2000.

The following table presents the changes in goodwill allocated to the Group's reportable segments:

	Pharmaceuticals £m	Consumer Healthcare £m	Total £m
At 1st January 2005	15,672	2,449	18,121
Additions	528	–	528
Disposals	(1)	–	(1)
Exchange adjustments	5	19	24
At 31st December 2005	16,204	2,468	18,672
Additions	16	116	132
Exchange adjustments	(76)	(21)	(97)
At 31st December 2006	16,144	2,563	18,707

(b) Intangible assets

The following tables set out the IFRS to US GAAP adjustments required to the IFRS income statement and balance sheet in respect of intangible assets:

Income statement	2006 £m	2005 £m	2004 £m
Amortisation charge under IFRS	139	109	75
Amortisation charge under US GAAP	1,454	1,674	1,516
IFRS to US GAAP adjustment for amortisation	1,315	1,565	1,441
Impairment charge under IFRS	80	99	26
Impairment charge under US GAAP	41	118	26
IFRS to US GAAP adjustment for impairment	(39)	19	–

In addition to the above adjustments for amortisation and impairments, further IFRS to US GAAP adjustments arose during the year of £125 million (2005 – £98 million; 2004 – £173 million) in respect of the acquisition and disposal of in-process R&D, licences, patents etc. which are capitalised under IFRS but charged directly to research and development expense under US GAAP, and £nil (2005 – £nil; 2004 – £37 million) in respect of disposals of product rights which have a higher carrying value under US GAAP than under IFRS.

Notes to the financial statements

continued

41 Reconciliation to US accounting principles continued

	2006 £m	2005 £m
Balance sheet		
Product rights intangible assets under IFRS	3,046	3,120
Product rights intangible assets under US GAAP	13,680	15,185
Net IFRS to US GAAP adjustment for product rights intangible assets	10,634	12,065

Product rights intangible assets under US GAAP are analysed as follows:

	Acquired products, licences, patents, etc. £m	Brands subject to amortisation £m	Indefinite lived brands £m	Total £m
2006				
Cost	21,249	1,096	4,811	27,156
Accumulated amortisation and impairment	(12,606)	(210)	(660)	(13,476)
Carrying value	8,643	886	4,151	13,680
2005				
Cost	21,369	1,096	4,722	27,187
Accumulated amortisation and impairment	(11,187)	(185)	(630)	(12,002)
Carrying value	10,182	911	4,092	15,185

The acquired products, licences and patents are pharmaceutical products, principally arising from the acquisition of SmithKline Beecham plc, and consumer healthcare products with book values net of accumulated amortisation and impairment as follows:

	2006 £m	2005 £m
<i>Avandia</i>	3,492	3,841
<i>Seroxat/Paxil</i>	940	1,410
<i>Augmentin</i>	966	1,142
<i>Fluviral</i>	571	683
<i>Havrix</i>	338	363
<i>Infanrix</i>	275	294
<i>Fraxiparine</i>	222	239
<i>Twinrix</i>	219	235
<i>Engerix-B</i>	209	224
<i>Hycamtin</i>	177	212
<i>Coreg</i>	122	240
Others	1,112	1,299
Acquired products, licences, patents etc. intangible assets under US GAAP	8,643	10,182

The indefinite lived brands relate to a large number of Consumer Healthcare products, principally arising from the acquisitions of SmithKline Beecham plc (including products previously acquired by SmithKline Beecham from Sterling Winthrop Inc.) and the Block Drug Company, with book values as follows:

	2006 £m	2005 £m
<i>Panadol</i>	683	730
<i>Aquafresh</i>	347	347
<i>Lucozade</i>	324	324
<i>Horlicks</i>	319	319
<i>Ribena</i>	309	309
<i>Nicorette</i>	292	292
<i>Odol</i>	228	228
<i>Tums</i>	226	226
<i>Nicoderm</i>	224	224
<i>Sensodyne</i>	216	225
Others	983	868
Indefinite lived brands intangible assets under US GAAP	4,151	4,092

41 Reconciliation to US accounting principles continued

Each of these brands is considered to have an indefinite life, given the strength and durability of the brand and the level of marketing support. The brands are in relatively stable and profitable market sectors, and their size, diversification and market shares mean that the risk of market-related factors causing a shortening of the brands' lives is considered to be relatively low. The Group is not aware of any material legal, regulatory, contractual, competitive, economic or other factor which could limit their useful lives. Accordingly, they are not amortised. Each brand is tested annually for impairment applying a fair value less costs to sell methodology and using five year post-tax cash flow forecasts with a terminal value calculation and applying a discount rate of the Group post-tax weighted average cost of capital of 8%, adjusted where appropriate for country-specific risks.

The carrying values of certain intangibles subject to amortisation were reviewed and an impairment of £6 million (2005 – £68 million) has been recorded. Of this, £6 million (2005 – £46 million) relates to pharmaceutical products and £nil (2005 – £22 million) to Consumer Healthcare products. An impairment charge in respect of Consumer Healthcare intangible assets not subject to amortisation of £35 million was recognised during 2006 (2005 – £50 million).

As discussed in Note 43 'Legal proceedings', a number of distributors of generic drugs have filed applications to market generic versions of a number of the Group's products prior to the expiration of the Group's patents. If generic versions of products are launched in future periods at earlier dates than the Group currently expects, impairments of the carrying value of the products may arise.

The estimated future amortisation expense for the next five years for intangible assets subject to amortisation as of 31st December 2006 is as follows:

Year	£m
2007	1,424
2008	1,241
2009	865
2010	846
2011	815
Total	5,191

In-process R&D of £14 million (2005 – £26 million; 2004 – £nil) arising on the acquisitions of CNS and Pliva in 2006 and ID Biomedical and Corixa in 2005 has been written off. This has been valued on the same basis as the other intangible assets acquired and relates to various development projects in the pre-approval stage where the technological feasibility of the projects had not been established at the point of acquisition.

(c) Theravance

In May 2004, the Group formed a strategic alliance with Theravance Inc. to develop and commercialise novel medicines across a variety of important therapeutic areas. Under the terms of the alliance, Theravance received \$129 million, a significant part of which related to the Group's purchase of Theravance shares. The Group has a call option in 2007 to further increase its ownership to over 50% at a significant premium to the price paid in the 2004 transaction. Theravance's other shareholders have a put option at a lower exercise price to cause GlaxoSmithKline to acquire up to half of the outstanding stock in 2007. Given the maximum number of shares subject to the put option, the Group's obligation is capped at \$525 million. The Group has an exclusive option to license potential new medicines from all of Theravance's programmes until August 2007. Upon exercising its option over a Theravance programme, the Group will be responsible for the relevant development, manufacturing and commercialisation activities. Depending on the success of such programmes, Theravance will receive clinical, regulatory and commercial milestone payments and royalties on the subsequent sales of medicines. Based on the assessment performed in May 2004, the Group was the primary beneficiary of Theravance, as defined by FIN 46R, and as a result Theravance was consolidated into the Group's US GAAP financial statements from that date. The net assets acquired were measured at fair value. The principal adjustment to the carrying value of the net assets in Theravance's balance sheet prior to the acquisition was recognition of in-process research and development (IPR&D) at a valuation of £273 million. The IPR&D was written off immediately after the acquisition in accordance with US GAAP purchase accounting.

In February 2006, Theravance completed a secondary offering of common stock, which is a reconsideration event as defined by FIN 46R. The assessment at this date indicated that the Group is no longer the primary beneficiary of Theravance's variable interests. Accordingly, Theravance has been de-consolidated from the Group's results under US GAAP since February 2006.

Additionally, the Group previously accounted for the Theravance put option discussed above in accordance with SFAS 150, 'Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity', which requires the Group to record the fair value of the put option as a liability. Since Theravance ceased to be a subsidiary of the Group under FIN 46R in February 2006, the put option has been accounted for in accordance with SFAS 133, 'Accounting for Derivative Instruments and Hedging Activities'. This also requires the fair value of the put option to be recorded as a liability. The fair value of the Theravance put option at 31st December 2006 is £10 million (2005 – £47 million). In accordance with SFAS 133, the call option is not recognised in the financial statements as it is not readily convertible into cash.

Notes to the financial statements

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41 Reconciliation to US accounting principles continued

(d) Taxation

	2006 £m	2005 £m	2004 £m
Total tax expense			
IFRS:			
Current tax expense	2,710	2,019	1,667
Deferred tax (credit)/expense	(409)	(103)	90
Total tax expense	2,301	1,916	1,757
US GAAP:			
Current tax expense	2,735	2,103	1,717
Deferred tax credit	(685)	(688)	(667)
Total tax expense	2,050	1,415	1,050
IFRS to US GAAP adjustments:			
Current tax expense	25	84	50
Deferred tax credit	(276)	(585)	(757)
Total tax expense	(251)	(501)	(707)

The IFRS to US GAAP adjustment in respect of current tax expense includes £41 million (2005 – £37 million; 2004 – £40 million) for the Group's share of the tax expense of associates. This is recognised in the Taxation charge in the income statement under US GAAP but recorded in Share of after tax profits of associates in the income statement presented in accordance with IFRS.

(e) Deferred taxation under US GAAP

	2006 £m	2005 £m
Liabilities		
Stock valuation adjustment	(44)	(42)
Other timing differences	20	63
Current deferred taxation liabilities	(24)	21
Accelerated capital allowances	(564)	(187)
Product rights	(3,563)	(4,035)
Product and business disposals	(1)	13
Pensions and other post-retirement benefits	317	25
Tax losses	80	–
Legal and other disputes	6	–
Manufacturing restructuring	37	–
Share option and award schemes	62	–
Other timing differences	8	25
Valuation allowances	(46)	–
Total deferred taxation liabilities	(3,688)	(4,138)
Assets		
Intra-Group profit	696	619
Stock valuation adjustment	(28)	(72)
Other timing differences	360	614
Current deferred taxation assets	1,028	1,161
Accelerated capital allowances	(33)	(492)
Product rights	(49)	(9)
Pensions and other post-retirement benefits	410	43
Tax losses	1,205	125
Restructuring	26	53
Legal and other disputes	147	160
Share option and award schemes	233	276
Other timing differences	128	(3)
Valuation allowances	(1,141)	(62)
Total deferred taxation assets	1,954	1,252

41 Reconciliation to US accounting principles continued**(e) Deferred taxation under US GAAP** continued

	2006 £m	2005 £m
Net deferred taxation under US GAAP	(1,734)	(2,886)
Net deferred taxation under IFRS	1,528	1,645
IFRS to US GAAP adjustment	(3,262)	(4,531)

(f) Pensions and post-retirement costs under US GAAP

	2006 £m	2005 £m	2004 £m
UK pension schemes	258	218	225
US pension schemes	61	55	54
Other overseas pension schemes	102	87	77
Unfunded post-retirement healthcare schemes	127	114	96
Post-employment costs	1	2	18
	549	476	470
Analysed as:			
Funded defined benefit/hybrid schemes	363	306	298
Unfunded defined benefit schemes	30	29	37
Defined contribution schemes	28	25	21
Unfunded post-retirement healthcare schemes	127	114	96
Post-employment costs	1	2	18
	549	476	470

The disclosures below include the additional information required by SFAS 132R and SFAS 158. The pension costs of the UK, US and major overseas defined benefit pension plans have been restated in the following tables in accordance with US GAAP. Minor retirement plans with pension costs in 2006 of £5 million (2005 – £8 million; 2004 – £5 million), have not been recalculated in accordance with the requirements of SFAS 87, and have been excluded.

Net periodic pension cost for the major retirement plans	2006 £m	2005 £m	2004 £m
Service cost	247	223	213
Interest cost	448	408	400
Expected return on plan assets	(491)	(444)	(431)
Amortisation of prior service cost	16	13	14
Amortisation of transition obligation	2	2	2
Amortisation of net actuarial loss	146	107	115
Net periodic pension cost under US GAAP	368	309	313
Termination benefits and curtailment costs	19	19	13

The assumptions used under IAS 19 within Note 26, are similar to those disclosed in the following table, which are presented on a weighted average basis.

Major assumptions used in computing pension costs	2006 % pa	2005 % pa	2004 % pa
Rates of future pay increases	4.25	4.00	4.25
Discount rate	5.00	4.75	5.25
Expected long-term rates of return on plan assets	6.75	6.75	7.00

In aggregate, average international plan assumptions did not vary significantly from US assumptions.

Estimated future benefit payments	£m
2007	355
2008	368
2009	385
2010	400
2011	416
2012–2016	2,386

Notes to the financial statements

continued

41 Reconciliation to US accounting principles continued

	2006 £m	2005 £m
Change in benefit obligation		
Benefit obligation at 1st January	(9,997)	(8,171)
Amendments	(36)	(1)
Service cost	(247)	(223)
Interest cost	(448)	(408)
Plan participants' contributions	(14)	(15)
Actuarial loss	(43)	(1,334)
Benefits paid	368	372
Termination benefits and curtailment costs	(17)	(15)
Exchange adjustments	263	(202)
Benefit obligation at 31st December	(10,171)	(9,997)
Benefit obligation at 31st December for pension plans with accumulated benefit obligations in excess of plan assets	(6,643)	(8,748)

The accumulated benefit obligation at 31st December 2006 was £9,385 million (2005 – £9,294 million).

	2006 £m	2005 £m
Change in plan assets		
Fair value of plan assets at 1st January	8,298	6,690
Actual return on plan assets	867	1,113
Employer contributions	592	661
Plan participants' contributions	14	15
Benefits paid	(368)	(372)
Exchange adjustments	(262)	191
Fair value of plan assets at 31st December	9,141	8,298
Fair value of plan assets at end of year for pension plans with accumulated benefit obligations in excess of plan assets	6,214	7,735

Plan assets consist primarily of investments in UK and overseas equities, fixed interest securities, index-linked securities and property. At 31st December 2006 UK equities included 0.1 million GSK shares (2005 – 1.9 million shares) with a market value of £1 million (2005 – £28 million). An analysis of the proportions of total plan assets for each major category is disclosed in Note 26. That analysis includes assets valued at £125 million in minor retirement plans, which have been excluded from these US GAAP tables.

	2006 £m	2005 £m
Funded status before adoption of SFAS 158		
Funded status	(1,030)	(1,699)
Unrecognised net actuarial loss	1,966	2,499
Unrecognised prior service cost	81	60
Unrecognised transition obligation	16	21
Net amount recognised before adoption of SFAS 158	1,033	881

	2006 £m	2005 £m
Amounts recognised in the statement of financial position before adoption of SFAS 158		
Prepaid benefit cost	423	8
Accrued pension liability	(460)	(1,027)
Intangible asset	100	86
Accumulated other comprehensive income	970	1,814
Net amount recognised before adoption of SFAS 158	1,033	881

41 Reconciliation to US accounting principles continued

Amount recognised in the statement of financial position	Before adoption of SFAS 158 £m	Incremental effect of SFAS 158 £m	After adoption of SFAS 158 £m
Prepaid/accrued	(37)	(993)	(1,030)
Intangible asset	100	(100)	–
Deferred tax asset	319	–	319
Accumulated other comprehensive income, net of deferred tax	651	1,093	1,744
At 31st December 2006	1,033	–	1,033

Amounts estimated to be recognised in net periodic pension cost in 2007	Total £m
Net actuarial loss	108
Prior service cost	17
Transition obligation	2
	127

Post-retirement healthcare under US GAAP

The post-retirement healthcare costs of the UK, US and major overseas post-retirement healthcare schemes have been restated in the following tables in accordance with US GAAP. Minor healthcare plans with costs in 2006 of £8 million (2005 – £5 million; 2004 – £nil) have not been recalculated and have been excluded.

Net healthcare cost	2006 £m	2005 £m	2004 £m
Service cost	35	37	32
Interest cost	62	57	55
Amortisation of prior service cost	(1)	(2)	(1)
Amortisation of net actuarial loss	22	15	11
Net healthcare cost	118	107	97

The major assumptions used in calculating the net healthcare cost were:

	%pa	%pa	%pa
Rate of future healthcare inflation	9.25 to 5.0	10.0 to 5.0	9.0 to 5.0
Discount rate	5.75	5.50	5.75

Change in benefit obligation	2006 £m	2005 £m
Benefit obligation at 1st January	1,211	965
Amendments	(16)	–
Service cost	35	37
Interest cost	62	57
Plan participants' contributions	8	8
Actuarial (gain)/loss	(117)	82
Benefits paid	(53)	(43)
Exchange	(102)	105
Benefit obligation at 31st December	1,028	1,211

Change in plan assets

Fair value of plan assets at 1st January	–	–
Employer and plan participants' contributions	53	43
Benefits paid	(53)	(43)
Fair value of plan assets at 31st December	–	–

Notes to the financial statements

continued

41 Reconciliation to US accounting principles continued

	2006 £m	2005 £m
Funded status before adoption of SFAS 158		
Funded status	(1,028)	(1,211)
Unrecognised net actuarial loss	265	450
Unrecognised prior service cost	(27)	(14)
Accrued post-retirement healthcare cost before adoption of SFAS 158	(790)	(775)

Amount recognised in the statement of financial position before adoption of SFAS 158

Accrued benefit cost	(790)	(775)
Accrued post-retirement healthcare cost before adoption of SFAS 158	(790)	(775)

Amount recognised in the statement of financial position

	Before adoption of SFAS 158 £m	Incremental effect of SFAS 158 £m	After adoption of SFAS 158 £m
Prepaid/accrued	(790)	(238)	(1,028)
Deferred tax asset	408	–	408
Accumulated other comprehensive income, net of deferred tax	(408)	238	(170)
At 31st December 2006	(790)	–	(790)

Amounts estimated to be recognised in net periodic pension cost in 2007

	Total £m
Net actuarial loss	13
Prior service cost	(2)
	11

Impact of a 1% variation in the assumed rate of future healthcare inflation

	1% decrease £m	1% increase £m
Effect on total service and interest cost for post-retirement healthcare	(7)	8
Effect on obligation for post-retirement healthcare	(75)	89

Estimated future benefit payments

	Gross £m	Medicare subsidy £m	Net £m
2007	46	(3)	43
2008	50	(4)	46
2009	55	(4)	51
2010	59	(5)	54
2011	62	(5)	57
2012-2016	354	(33)	321

42 Principal Group companies

The following represent the principal subsidiary and associated undertakings of the GlaxoSmithKline Group at 31st December 2006. Details are given of the principal country of operation, the location of the headquarters, the business segment and the business activities. The equity share capital of these undertakings is wholly owned by the Group except where its percentage interest is shown otherwise. All companies are incorporated in their principal country of operation except where stated.

Europe	Location	Subsidiary undertaking	Segment	Activity	%
England	Brentford	+GlaxoSmithKline Holdings Limited	Ph,CH	h	
	Brentford	+GlaxoSmithKline Holdings (One) Limited	Ph,CH	h	
	Brentford	+GlaxoSmithKline Services Unlimited	Ph,CH	s	
	Brentford	GlaxoSmithKline Finance plc	Ph,CH	f	
	Brentford	GlaxoSmithKline Capital plc	Ph	f	
	Brentford	SmithKline Beecham p.l.c.	Ph,CH	d e h m p r	
	Brentford	Wellcome Limited	Ph,CH	h	
	Greenford	Glaxo Group Limited	Ph	h	
	Greenford	Glaxo Operations UK Limited	Ph	p	
	Brentford	Glaxo Wellcome International B.V. (i)	Ph,CH	h	
	Brentford	Glaxo Wellcome Investments B.V. (i)	Ph,CH	h	
	Stockley Park	Glaxo Wellcome UK Limited	Ph	h m p	
	Brentford	GlaxoSmithKline Export Limited	Ph	e	
	Brentford	GlaxoSmithKline Research & Development Limited	Ph	d r	
	Brentford	GlaxoSmithKline UK Limited	Ph	m p	
	Brentford	SmithKline Beecham (Investments) Limited	Ph,CH	f	
	Brentford	SmithKline Beecham (SWG) Limited	CH	e m	
	Brentford	Setfirst Limited	Ph,CH	h	
	Greenford	The Wellcome Foundation Limited	Ph	p	
	Austria	Vienna	GlaxoSmithKline Pharma G.m.b.H	Ph	m
Belgium	Genval	GlaxoSmithKline S.A.	Ph	m	
	Rixensart	GlaxoSmithKline Biologicals S.A.	Ph	d e m p r	
	Rixensart	GlaxoSmithKline Biologicals Manufacturing S.A.	Ph	h	
Czech Republic	Prague	GlaxoSmithKline s.r.o.	Ph,CH	m	
Denmark	Ballerup	GlaxoSmithKline Consumer Healthcare A/S	CH	m	
	Brøndby	GlaxoSmithKline Pharma A/S	Ph	m	
Finland	Espoo	GlaxoSmithKline Oy	Ph	m	
France	Marly le Roi	Groupe GlaxoSmithKline S.A.S.	Ph	h	
	Marly le Roi	Laboratoire GlaxoSmithKline S.A.S.	Ph	m	
	Marly le Roi	Glaxo Wellcome Production S.A.S.	Ph	m p	
	Marly le Roi	GlaxoSmithKline Sante Grand Public S.A.S.	CH	m	
Germany	Buehl	GlaxoSmithKline Consumer Healthcare GmbH & Co. KG	CH	d h m p r s	
	Munich	GlaxoSmithKline Pharma GmbH	Ph	h	
Greece	Athens	GlaxoSmithKline A.E.B.E	Ph,CH	h m	
Guernsey	St. Peter Port	SmithKline Beecham Limited	Ph,CH	i	
	St. Peter Port	Setfirst (No.2) Limited	Ph,CH	h	
Hungary	Budapest	GlaxoSmithKline Medicine and Healthcare Products Limited	Ph,CH	e m	
Italy	Verona	GlaxoSmithKline S.p.A.	Ph	d h m r	
	Milan	GlaxoSmithKline Consumer Healthcare S.p.A.	CH	h m	
Luxembourg	Mamer	GlaxoSmithKline International (Luxembourg) S.A.	Ph,CH	f h	

Notes to the financial statements

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42 Principal Group companies continued

Europe	Location	Subsidiary undertaking	Segment	Activity	%
Netherlands	Zeist	GlaxoSmithKline B.V.	Ph	m	
	Zeist	GlaxoSmithKline Consumer Healthcare B.V.	CH	m	
Norway	Oslo	GlaxoSmithKline AS	Ph	m	
Poland	Poznan	GlaxoSmithKline Pharmaceuticals S.A.	Ph	m p	97
	Poznan	GSK Services Sp.z.o.o	Ph	m	
	Warsaw	GlaxoSmithKline Consumer Healthcare Sp.z.o.o.	CH	m e	
Portugal	Alges	GlaxoSmithKline-Produtos Farmaceuticos, Limitada	Ph	m	
Republic of Ireland	Carrigaline	SmithKline Beecham (Cork) Limited (ii)	Ph	p	
	Carrigaline	GlaxoSmithKline Trading Services Limited (ii)	Ph	e	
	Dublin	GlaxoSmithKline Consumer Healthcare (Ireland) Limited (ii)	CH	m	
Russian Federation	Moscow	GlaxoSmithKline Trading	Ph	m	
Spain	Madrid	GlaxoSmithKline S.A.	Ph	m p	
	Madrid	GlaxoSmithKline Consumer Healthcare S.A.	CH	m	
Sweden	Solna	GlaxoSmithKline AB	Ph	m	
Switzerland	Muenchenbuchsee	GlaxoSmithKline AG	Ph	m	
USA					
USA	Hamilton	Corixa Corporation	Ph	m p	
	Minneapolis	CNS, Inc.	CH	m p	
	Philadelphia	SmithKline Beecham Corporation	Ph,CH	d e h m p r s	
	Pittsburgh	GlaxoSmithKline Consumer Healthcare, L.P.	CH	m p	88
	Pittsburgh	Block Drug Company, Inc.	CH	h m p	
	Wilmington	GlaxoSmithKline Holdings (Americas) Inc.	Ph,CH	h	
Americas					
Bermuda	Hamilton	GlaxoSmithKline Insurance Ltd	Ph,CH	i	
Canada	Mississauga	GlaxoSmithKline Inc.	Ph	m p r	
	Oakville	GlaxoSmithKline Consumer Healthcare Inc.	CH	m	
	Laval	ID Biomedical Corporation	Ph	d m p r	
Asia Pacific					
Australia	Boronia	Glaxo Wellcome Australia Pty Ltd	Ph,CH	d e m p r	
China	Hong Kong	GlaxoSmithKline Limited	Ph,CH	m	
	Tianjin	Sino-American Tianjin Smith Kline & French Laboratories Ltd	Ph	d m p r	55
India	Mumbai	GlaxoSmithKline Pharmaceuticals Limited	Ph	m p	51
	Nabha	GlaxoSmithKline Consumer Healthcare Limited (iii)	CH	m p	43
Malaysia	Petaling Jaya	GlaxoSmithKline Pharmaceutical Sdn Bhd	Ph	m	
New Zealand	Auckland	GlaxoSmithKline NZ Limited	Ph,CH	m	
Pakistan	Karachi	GlaxoSmithKline Pakistan Limited	Ph,CH	m p e	79
Philippines	Makati	GlaxoSmithKline Philippines Inc	Ph,CH	m	
Singapore	Singapore	Glaxo Wellcome Manufacturing Pte Ltd	Ph	p	
	Singapore	GlaxoSmithKline Pte Ltd	Ph	m	
South Korea	Seoul	GlaxoSmithKline Korea	Ph	m p	
Taiwan	Taipei	Glaxo Wellcome Taiwan Limited	Ph	m p	

42 Principal Group companies continued

Japan	Location	Subsidiary undertaking	Segment	Activity	%
Japan	Tokyo	GlaxoSmithKline K.K.	Ph,CH	d m p r	

Latin America

Argentina	Buenos Aires	GlaxoSmithKline Argentina S.A.	Ph,CH	m p	
Brazil	Rio de Janeiro	GlaxoSmithKline Brasil Ltda	Ph,CH	m p	
Colombia	Bogota	GlaxoSmithKline Colombia S.A.	Ph,CH	m	
Mexico	Delegacion Tlalpan	GlaxoSmithKline Mexico S.A. de C.V.	Ph,CH	e m p s	
Puerto Rico	Guaynabo	GlaxoSmithKline Puerto Rico Inc.	Ph	m	
	San Juan	SB Pharmco Puerto Rico Inc.	Ph	p	
Venezuela	Caracas	GlaxoSmithKline Venezuela C.A.	Ph,CH	m	

Middle East & Africa

Egypt	Cairo	GlaxoSmithKline S.A.E	Ph	m p	91
South Africa	Bryanston	GlaxoSmithKline South Africa (Pty) Ltd	Ph,CH	m p	
Turkey	Istanbul	GlaxoSmithKline Ilaclari Sanayi ve Ticaret A.S.	Ph	m p	

USA	Location	Associated undertaking	Business	%
USA	Teterboro	Quest Diagnostics Incorporated (iv)	Clinical testing	19

- i) Incorporated in the Netherlands.
 - ii) Exempt from the provisions of Section 7 of the Companies (Amendment) Act 1986 (Ireland).
 - iii) Consolidated as a subsidiary undertaking in accordance with Section 258 (4)(a) of the Companies Act on the grounds of dominant influence.
 - iv) Equity accounted on the grounds of significant influence.
- + Directly held wholly owned subsidiary of GlaxoSmithKline plc.

Key

Business segment: Ph Pharmaceuticals, CH Consumer Healthcare

Business activity: d development, e exporting, f finance, h holding company, i insurance, m marketing, p production, r research, s service

Full details of all Group subsidiary and associated undertakings will be attached to the company's Annual Return to be filed with the Registrar of Companies.

Notes to the financial statements

continued

43 Legal proceedings

The Group is involved in significant legal and administrative proceedings, principally product liability, intellectual property, tax, anti-trust and governmental investigations and related private litigation. The Group makes provision for these proceedings on a regular basis as summarised in Notes 2 and 27. The Group may make additional significant provisions for such legal proceedings as required in the event of further developments in these matters, consistent with generally accepted accounting principles. Litigation, particularly in the USA, is inherently unpredictable and excessive awards that may not be justified by the evidence may occur. The Group could in the future incur judgements or enter into settlements of claims that could result in payments that exceed its current provisions by an amount that would have a material adverse effect on the Group's financial condition, results of operations and/or cash flows.

Intellectual property claims include challenges to the validity of the Group's patents on various products or processes and assertions of non-infringement of those patents. A loss in any of these cases could result in loss of patent protection for the product at issue. The consequences of any such loss could be a significant decrease in sales of that product and could materially affect future results of operations for the Group.

Legal expenses incurred and provisions related to legal claims are charged to selling, general and administration costs. Provisions are made, after taking appropriate legal and other specialist advice, when a reasonable estimate can be made of the likely outcome of the dispute. Beginning in 2004, the Group has established an actuarially determined provision for product liability claims incurred but not yet reported as described in Note 27. At 31st December 2006, the Group's aggregate provision for legal and other disputes (not including tax matters described under 'Taxation' in Note 12) was over £1 billion. The ultimate liability for legal claims may vary from the amounts provided and is dependent upon the outcome of litigation proceedings, investigations and possible settlement negotiations.

The most significant of those matters are described below.

Intellectual property

Advair

In September 2004, the Group applied to the US Patent and Trademark Office (USPTO) for re-issue of its combination patent for *Advair*, an inhaled combination of salmeterol and fluticasone propionate, which expires in September 2010. This followed an internal review which concluded that the language in the patent may not accurately describe all of the circumstances of the invention and may not claim the invention as precisely as it could. The objective of seeking re-issuance is to strengthen the protection afforded by the patent. In January 2007, the Group received a Notice of Allowance finding the pharmaceutical composition claims patentable. The re-issued patent will have the same September 2010 expiration date as the original composition patent and will be listed in the register of pharmaceutical patents maintained by the US Food and Drug Administration (FDA) (the Orange Book).

The Group holds other US patents relating to *Advair*, including various patents relating to the *Diskus* device which expire over a period from 2011 to 2016, and various patents relating to the HFA formulation and MDI device which expire over a period from 2014 to 2017.

Avandia and Avandamet

In August 2003, the Group filed an action in the US District Court for the District of New Jersey against Teva Pharmaceuticals USA Inc. for infringement of the Group's patent relating to the maleate salt form of rosiglitazone, the active ingredient in *Avandia*, which expires in 2015. In September 2003, the Group filed a comparable action in same court against Dr. Reddy's Laboratories, alleging infringement of the same patent. Those actions were filed in response to Abbreviated New Drug Application (ANDA) filings with the FDA by Dr. Reddy's Laboratories and Teva with certifications that the Group's maleate salt patent is invalid. Teva subsequently filed an additional certification challenging the validity of the Group's basic compound patent for rosiglitazone, and in January 2004 the Group commenced an action against Teva in the same court for infringement of that patent. The basic compound patent currently expires in 2012 after giving effect to patent term restoration and paediatric exclusivity. The actions have been consolidated and a trial date set for 6th August 2007 for the Group's actions against Teva on the basic compound and maleate salt patents and Dr. Reddy's on the maleate salt patent.

Both Teva and Dr. Reddy's have tentative FDA approval for all dosage strengths. The Hatch-Waxman stays against final FDA approval in respect of the ANDAs filed by both companies expired in November 2006.

In January 2005, the Group filed an action in the US District Court for the District of New Jersey against Teva for infringement of the same two patents – the basic compound and maleate salt patents for rosiglitazone. Teva had filed an ANDA with the FDA for a generic version of *Avandamet* with a certification that those patents are invalid or not infringed. FDA approval of that ANDA is stayed until the earlier of June 2007 or resolution of the patent infringement action. Since *Avandamet* is protected by the same patents as *Avandia*, any earlier holding of invalidity in the *Avandia* cases would be dispositive for *Avandamet* as well.

Imitrex

In December 2003, the Group commenced an action in the US District Court for the Southern District of New York against Dr. Reddy's Laboratories, alleging infringement of one of the two primary compound patents for sumatriptan, the active ingredient in *Imitrex*. The patent at issue affords protection through February 2009 after giving effect to a grant of paediatric exclusivity by the FDA. The defendant had filed an ANDA with the FDA for sumatriptan oral tablets with a certification of invalidity of that compound patent but did not certify invalidity or non-infringement of the other compound patent that expires in June 2007 after giving effect to paediatric exclusivity.

In March 2004, the Group commenced an infringement action against Cobalt Pharmaceuticals which was transferred to the US District Court for the Southern District of New York. The defendant had filed an ANDA for sumatriptan oral tablets with a certification of invalidity or non-infringement of the same compound patent at issue in the Dr. Reddy's case.

In February 2005, the Group commenced an infringement action in the US District Court for the District of Delaware against Spectrum Pharmaceuticals. The defendant had filed an ANDA for injectable sumatriptan with a certification of invalidity or non-infringement of the same compound patent at issue in the Dr. Reddy's and Cobalt cases.

43 Legal proceedings continued

In October 2006, the Group reached a settlement agreement with Dr. Reddy's which provides that Dr. Reddy's may exclusively distribute authorised generic versions of sumatriptan tablets in the USA with an expected launch date late in the fourth quarter of 2008. In November 2006, the Group reached a settlement with Cobalt which provides that Cobalt may distribute a generic version of sumatriptan tablets in the USA with an expected launch date early in the first quarter of 2009. In December 2006, the Group reached a settlement with Spectrum which provides that Spectrum may exclusively distribute authorised versions of certain sumatriptan injection products in the USA with an expected launch during the Group's sumatriptan paediatric exclusivity period which begins in August 2008, with such launch occurring not later than early November 2008.

Lamictal

In August 2002, the Group commenced an action in the US District Court for the District of New Jersey against Teva Pharmaceuticals USA Inc., alleging infringement of the Group's compound patent for lamotrigine, the active ingredient in *Lamictal* oral tablets. That patent affords protection through January 2009 after giving effect to a grant of paediatric exclusivity by the FDA. Teva had filed an ANDA with the FDA with a certification of invalidity of the Group's patent. The parties reached a settlement agreement pursuant to which the Group has granted Teva an exclusive royalty-bearing license to distribute in the USA a generic version of lamotrigine chewable tablets. In addition, Teva was granted the exclusive right to manufacture and sell Teva's own generic version of lamotrigine tablets in the USA with an expected launch date in 2008.

Paxil/Seroxat

In the USA a number of distributors of generic drugs filed applications with the FDA to market generic versions of *Paxil/Seroxat* (paroxetine hydrochloride) prior to the expiration in 2007 of the Group's patent on paroxetine hydrochloride hemihydrate. Other distributors sought to bring to market anhydrate or other versions of paroxetine hydrochloride and in one case paroxetine mesylate. In response the Group filed actions against all those distributors for infringement of various of the Group's patents on the basis that the generic anhydrate and other versions infringe because they contain and/or convert to the hemihydrate form and/or infringe other Group patents.

In July 1998, the Group filed an action against Apotex in the US District Court for the Northern District of Illinois for infringement of the Group's patent for paroxetine hydrochloride hemihydrate. Apotex had filed an ANDA with the FDA seeking approval to introduce a generic form of *Paxil*. Following a trial in February 2003, the judge ruled the Group's patent valid but not infringed by Apotex's product. On the Group's appeal to the US Court of Appeals for the Federal Circuit (CAFC), which hears all appeals from US District Courts on patent matters, the CAFC ruled that the Group's patent was infringed but invalid based upon 'public use' in clinical trials prior to the filing date in the USA. The Group filed a petition to the CAFC for rehearing on its appeal by the full court and in April 2005 the full CAFC vacated that judgement and remanded the matter to the same panel. Concurrently with entry of that decision, the panel issued a new opinion ruling the same patent invalid under an alternative theory.

Between 1999 and 2001 the Group filed further actions against Apotex in the US District Court for the Eastern District of Pennsylvania for infringement of additional of the Group's patents. In December 2002, the judge granted in part and denied in part summary judgement motions filed by Apotex with the result that issues of validity and infringement of three of the four new patents remained for trial. In July 2004, the judge certified the patent that had been held invalid for appeal to the US Circuit Court for the CAFC. In February 2006, the CAFC affirmed the judge's ruling of invalidity of that patent.

The Group also commenced actions in the US District Court for the Eastern District of Pennsylvania against Geneva, Alphapharm, AndrX Pharmaceuticals, Zenith and Teva Pharmaceuticals in connection with their ANDA filings for *Paxil* and BASF and Sumika Fine Chemicals in connection with their supply of paroxetine hydrochloride for use in ANDAs. All the Group's patent infringement claims against these defendants have been resolved.

Apotex launched its generic product in the USA in September 2003. Additional generic products were launched by other defendants after March 2004.

The Group's US patent litigation with Synthon BV was settled in December 2003 enabling US marketing of Synthon's paroxetine mesylate product. This was followed with settlement in August 2004 of most of the Group's non-US patent litigation with Synthon as a consequence of which Synthon is free to market its paroxetine mesylate product in many markets globally where it has obtained marketing authorisations. Paroxetine mesylate is a different salt form of paroxetine than that used in the marketed form of *Seroxat/Paxil*. In certain markets litigation with Synthon is ongoing and Synthon is asserting counterclaims for unfair competition against the Group.

Generic products containing the anhydrate form of paroxetine hydrochloride are now on the market in most European countries. Whilst some of these products are the subject of continuing litigation, most actions have now been settled and it is expected that more will be settled in the future. In the UK, litigation of several years standing between the Group and Apotex culminated in an Appeal Court decision that the Group's anhydrate process patent was valid but not infringed. Following the litigation in Canada with Apotex over several other patents related to paroxetine, Apotex launched its generic product in Canada in October 2003. Apotex alleged that as a result of that litigation it had been enjoined from launching that product after receipt of regulatory approval. An action by Apotex to recover damages related to the delay occasioned by those injunctions is ongoing.

Paxil CR

In November 2005, Mylan Pharmaceuticals filed an ANDA for *Paxil CR* (paroxetine hydrochloride controlled release formulation) with a certification of invalidity and non-infringement of several patents listed in the FDA Orange Book. There was no certification of invalidity or non-infringement of the patent covering paroxetine hydrochloride hemihydrate, which Mylan admitted is the active ingredient in its product. That patent expires in June 2007, after giving effect to a grant of paediatric exclusivity by the FDA. As the Group did not file a patent infringement action against Mylan within the 45-day period provided under Hatch-Waxman, there is no 30-month stay of FDA approval of the Mylan ANDA.

Notes to the financial statements

continued

43 Legal proceedings continued

Requip

In April 2005, the Group commenced an action in the US District Court for the District of Delaware against Teva Pharmaceutical USA Inc. alleging infringement of the Group's compound patent for ropinirole hydrochloride (the active ingredient in *Requip*) and a method of use patent for treatment of Parkinson's disease, both of which are listed in the FDA Orange Book. The compound patent expires in December 2007 and the method of use patent in May 2008. The defendant filed an ANDA with the FDA with a certification of invalidity and non-infringement of those patents. FDA approval of that ANDA is stayed until the earlier of August 2007 or resolution of the patent infringement action. In December 2006, the judge ruled at the conclusion of the trial that the Group's method of use of ropinirole to treat Parkinson's Disease is novel and nonobvious rejecting Teva's claims on those grounds. Teva's further claim that the patent is unenforceable for inequitable conduct remains before the judge as the evidence was not reviewed at the trial. This issue is to be decided on the basis of deposition testimony and documents and consideration of further potential filings by the parties. Teva's original challenge to the Group's basic compound patent was withdrawn before trial, and Teva has accepted that the FDA will not approve its product prior to expiration of that patent.

Valtrex

In May 2003, the Group commenced an action in the US District Court for the District of New Jersey against Ranbaxy Laboratories, alleging infringement of the Group's compound patent for valacyclovir, the active ingredient in *Valtrex*. That patent expires in 2009. The defendant has filed an ANDA with the FDA with a certification the Group's compound patent was invalid or not infringed. In August 2004, Ranbaxy filed a motion for partial summary judgement that the patent was invalid for being in 'public use' more than one year before the filing of the patent application and the Group filed a motion that the patent was not invalid on those grounds. In March 2005, the court ruled in the Group's favour that the patent was not invalid on those grounds.

On 1st February 2007, Ranbaxy received FDA approval for its generic valacyclovir product and notified the Group that it sought to market the product in the USA. Under the terms of an earlier agreement between the companies, previously approved by the court, Ranbaxy had agreed that if the Group applied for a preliminary injunction within 45 days of that notification Ranbaxy would not launch its product until the court either ruled on the preliminary injunction or decided the pending court case. At a conference with the court on 28th February 2007 a trial date for the case was set for 7th August 2007 and the parties agreed that it would not be necessary that the Group file a request for a preliminary injunction.

Wellbutrin XL

In December 2004, Biovail commenced actions in the US District Court for the Central District of California against Anchen Pharmaceuticals and in the US District Court for the Southern District of Florida against Abrika Pharmaceuticals, in each case alleging infringement of Biovail formulation patents for *Wellbutrin XL*. In April 2005, Biovail filed an action in the US District Court for the Eastern District of Pennsylvania against Impax Laboratories for infringement of the same patents. Those patents expire in 2018. Each of Anchen, Abrika and Impax had filed an ANDA with the FDA with a certification of invalidity or non-infringement of the Biovail patents. The Group is the licensee under those patents. In August 2006, the judge granted Anchen's motion and ruled that Anchen's ANDA product did not infringe Biovail's patent. Biovail has appealed that decision to the CAFC. A hearing on Abrika's motion for summary judgement was heard in April 2006 but as of the date of this report no decision has been announced. Impax filed a motion for summary judgement of nonfringement in August 2006, but as of the date of this report no decision has been announced. The Group is not a party to any of those actions. In September 2005, Biovail commenced actions in the US District Court for the Southern District of New York against Watson Laboratories alleging infringement of the Biovail formulation patents. Watson's third party counterclaim against the Group based on listing activities associated with the FDA Orange Book was dismissed in October 2006.

The FDA has given final approval to Anchen's ANDA for its generic version of *Wellbutrin XL* and to Impax for a generic 300 mg tablet product. The 300 mg generic product was launched in the USA at the end of December 2006. No generic version of the 150 mg tablet has been launched as of the date of this report.

In December 2005, Andrx Pharmaceuticals filed an action against the Group in the US District Court for the Southern District of Florida, alleging that the manufacture, importation and sale of the 150 mg *Wellbutrin XL* product infringes a patent issued to Andrx in June 2005 and asking for treble damages, attorneys' fees and that the Group and others acting in concert with it be enjoined. In February 2007, the parties reached a settlement, providing that the Group pay Andrx a \$35 million license fee and that Andrx grant the Group a royalty-bearing license to its US patents covering *Wellbutrin XL*.

Zofran

In August 2001, the Group commenced an action in the US District Court for the District of New Jersey against Reddy-Cheminor and Dr. Reddy's Laboratories. Dr. Reddy had certified invalidity of three patents for ondansetron, the active ingredient in *Zofran* tablets, including the compound patent that expired in July 2005 and two method of use patents, the later of which expired in December 2006, in both instances taking into account the extension for paediatric exclusivity. In July 2003, the Group filed an action against Dr. Reddy's Laboratories in the same district court for infringement of the Group's patents related to the orally disintegrating tablet presentation of *Zofran*. In October 2003, the Group filed an action against West-ward Pharmaceuticals, Inc. in the same district court for infringement of the Group's patents related to an injectable presentation of *Zofran*. Both the Dr. Reddy's disintegrating tablet case and the West-ward case were consolidated with the earlier Dr. Reddy's case.

43 Legal proceedings continued

Prior to the trial both Reddy-Chemisor and West-ward withdrew their challenge to the compound patent. The trial over infringement and validity of the Group's method of use and process patents was completed in June 2004 and closing arguments were heard in May 2005. The parties subsequently reached a settlement agreement, the terms of which remain confidential.

In March 2002, the Group filed a similar action against Teva Pharmaceuticals USA Inc. in the US District Court for the District of Delaware alleging infringement of the two method of use patents for ondansetron. Teva had certified invalidity or non-infringement of the two method of use patents. Teva did not challenge the compound patent. The trial judge ruled in the Group's favour, upholding the validity of the method of use patents. Following an appeal by Teva to the CAFC, the parties reached a settlement agreement, the terms of which remain confidential.

In January 2003, the Group commenced an action against Kali Laboratories (now Par Pharmaceutical Company) in the US District Court for the District of New Jersey involving orally disintegrating *Zofran* tablets. The trial judge denied Kali's summary judgement motion and granted the Group's summary judgement motions in June 2005 and July 2005, affirming the validity of the Group's method of use patents and holding that Kali's proposed generic product would infringe those patents. Following an appeal by Kali to the CAFC, the parties reached a settlement agreement, the terms of which remain confidential.

Following the settlement agreements referred to above, generic ondansetron tablet products were launched by a number of distributors in the USA in December 2006.

Product liability

Pre-clinical and clinical trials are conducted during the development of potential products to determine the safety and efficacy of products for use by humans following approval by regulatory bodies. Notwithstanding these efforts, when drugs and vaccines are introduced into the marketplace, unanticipated side effects may become evident. The Group is currently a defendant in a number of product liability lawsuits related to the Group's pharmaceutical products. The most significant of those matters are described below.

Paxil

The Group has received lawsuits and claims filed on behalf of patients alleging that they have suffered symptoms on discontinuing treatment with *Paxil* (paroxetine). Separately, the Group has received lawsuits and claims that patients who had commenced *Paxil* treatment committed or attempted to commit suicide and/or acts of violence. The Group has also received lawsuits and claims alleging that use of *Paxil* during pregnancy resulted in the birth of a child with birth defects or health issues.

The Group received lawsuits filed in state and federal courts in the USA and Canada on behalf of thousands of plaintiffs, including purported class actions, alleging that paroxetine (the active ingredient in *Paxil*) is addictive and causes dependency and withdrawal reactions. Plaintiffs sought remedies including compensatory, punitive and statutory damages and the cost of a fund for medical monitoring. In 2003, a federal judge in the US District Court for the Central District of California denied class action certifications for a nationwide class and a California statewide class as to cases filed in federal court in that district. Subsequently, on petition from plaintiffs' counsel all federal court cases were transferred to that District Court for consolidation in Multidistrict Litigation (MDL). In January 2006, a conditional settlement agreement that included more than 90 per cent of the pending claims based on symptoms on discontinuing *Paxil* treatment became effective. The Group did not, as part of the settlement, admit any liability with respect to the allegations in any of the suits. Virtually all the personal injury lawsuits concerning discontinuation symptoms have now been resolved by settlement or dismissal. One purported class action consumer fraud lawsuit focused on discontinuation symptoms continues in California state court. There is also purported class action litigation in Canada concerning symptoms on discontinuation of *Paxil*.

The Group has received numerous claims and lawsuits alleging that treatment with *Paxil* has caused homicidal or suicidal behaviour exhibited by users of the product. Class certification was denied in January 2007 in the one purported personal injury class action lawsuit which is pending in the US District Court for the Eastern District of Pennsylvania. In January 2005, the FDA approved a black box warning that antidepressants increased the risk of suicidal thoughts or behaviour in paediatric patients and other strengthened warnings for selective serotonin reuptake inhibitor (SSRI) products, including *Paxil*, as a class. In May 2006, the *Paxil* US label was updated to warn that young adults, especially those with Major Depressive Disorder, may be at increased risk for suicidal behaviour during treatment with paroxetine. In December 2006, the FDA held an Advisory Committee meeting following a review of data regarding suicidal thoughts and behaviours in clinical studies of various antidepressants in adults. The FDA is expected to update the label for antidepressants as a class to advise of a possible increased risk for suicidal behaviour in young adults.

The Group has received numerous lawsuits and claims alleging that use of *Paxil* during the first trimester of pregnancy resulted in the birth of a child with a heart defect or other birth defect. The Group is also involved in litigation alleging that the use of *Paxil* during pregnancy resulted in the birth of a baby with primary pulmonary hypertension of the newborn. In September 2005, the US label for *Paxil* was updated to reflect new information that suggested an increased risk of congenital malformations (particularly cardiovascular malformations) in infants born to mothers who took *Paxil* during the first trimester of pregnancy. In December 2005, the *Paxil* US label was further updated to include new data and to strengthen the pregnancy warning from Category C to Category D, which indicates there is evidence of risk to the foetus, but the potential benefits from the use of the drug in pregnant women may outweigh the risk. In May 2006, the *Paxil* US label was again updated to include a class warning concerning persistent pulmonary hypertension of the newborn in mothers who took *Paxil* after the 20th week of pregnancy.

Notes to the financial statements

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43 Legal proceedings continued

Phenylpropanolamine

Following a report from the Yale Haemorrhagic Stroke Project that found a suggestion of an association between first use of phenylpropanolamine (PPA) decongestant and haemorrhagic stroke, the Group and most other manufacturers have voluntarily withdrawn consumer healthcare products in which PPA was an active ingredient. Since the PPA product withdrawal the Group has been named as a defendant in numerous personal injury and class action lawsuits filed in state and federal courts alleging personal injury or increased risk of injury from use of products containing PPA and unfair and deceptive business practices. Plaintiffs seek remedies including compensatory and punitive damages and refunds.

The federal cases have been consolidated in a multidistrict litigation proceeding in the US District Court for the District of Washington. The judge responsible for those proceedings has denied class certification and struck all class allegations in the federal personal injury and consumer refund class actions. Class certification has been denied in California state court and a Pennsylvania state court putative class action has been dismissed, leaving no putative class actions pending against the Group in this litigation. A substantial number of cases in which the Group or other manufacturers are defendants have reached trial in state and federal courts. Manufacturers have for the most part received favourable outcomes at trial.

Baycol

In August 2001, Bayer AG withdrew *Baycol* (cerivastatin sodium) worldwide in light of reports of adverse events, including deaths, involving rhabdomyolysis. The Group had participated in the marketing of *Baycol* in the USA pursuant to a co-promotion agreement with Bayer which was the licence holder and manufacturer of the product.

Following the withdrawal, Bayer and the Group have been named as defendants in thousands of lawsuits filed in state and federal courts in the USA on behalf of both individuals and putative classes of former *Baycol* users. A number of the suits allege that the plaintiffs have suffered personal injuries, including rhabdomyolysis, from the use of *Baycol*. Others claim that persons who took *Baycol*, although not injured, may be at risk of future injury or may have suffered economic damages from purchasing and using *Baycol*. Plaintiffs seek remedies including compensatory, punitive and statutory damages and creation of funds for medical monitoring.

The Group and Bayer Corporation, the principal US subsidiary of Bayer AG, have signed an allocation agreement under which Bayer Corporation has agreed to pay 95 per cent of all settlements and compensatory damages judgements with each party retaining responsibility for its own attorneys' fees and any punitive damages. The federal cases have been consolidated in a MDL proceeding in the US District Court for the District of Minnesota. To date two statewide class actions have been certified – a medical monitoring case in Pennsylvania and a Consumer Fraud and Deceptive Business Practices Act case in Illinois. The medical monitoring action was dismissed by the court on summary judgement. Another class action, in which GSK was not named as a defendant, has been certified in Oklahoma. A substantial number of claims for death or serious injury have been settled and many others alleging muscle aches and pains have been voluntarily or involuntarily dismissed.

Fen-Phen

In 1997, the FDA became aware of reports of cardiac valvular problems in individuals for whom fenfluramine or dexfenfluramine alone or in combination with phentermine was prescribed as part of a regimen of weight reduction and requested the voluntary withdrawal of fenfluramine and dexfenfluramine from the market. The reports of cardiac valvular problems and the subsequent withdrawal of those products from the market spawned numerous product liability lawsuits filed against the manufacturers and distributors of fenfluramine, dexfenfluramine and phentermine. As one of a number of manufacturers of phentermine, the Group remains a defendant in less than one hundred of several thousand lawsuits that were filed in various state and federal district courts in the USA against the Group and other defendants.

Most of the lawsuits seek relief including some combination of compensatory and punitive damages, medical monitoring and refunds for purchases of drugs. In 1997, the Judicial Panel on Multidistrict Litigation issued an order consolidating and transferring all federal actions to the US District Court for the Eastern District of Pennsylvania. That court approved a global settlement proposed by defendant Wyeth, which sold fenfluramine and dexfenfluramine. The settlement, subsequently approved by the Third Circuit Court of Appeals, does not include any of the phentermine defendants, including the Group. Individual plaintiffs may elect to opt out of the class settlement and pursue their claims individually and tens of thousands of plaintiffs have elected to do so. Wyeth continues to settle individual state court cases before trial and the Group continues to be dismissed from lawsuits as they are settled by Wyeth.

Thimerosal

The Group, along with a number of other pharmaceutical companies, has been named as a defendant in numerous individual personal injury lawsuits in state and federal district courts in the USA alleging that thimerosal, a preservative used in the manufacture of vaccines, causes neurodevelopmental disorders and other injuries, including autism. Two of the cases are purported class actions although there has been no determination whether any of those cases will be permitted to proceed as a class action. A number of purported class actions in other jurisdictions have been withdrawn or dismissed. Plaintiffs seek remedies including compensatory, punitive and statutory damages and the cost of a fund for medical monitoring and research. As of the date of this report there are no cases scheduled for trial in 2007 in which the Group is a defendant.

43 Legal proceedings continued**Sales and marketing and regulation****Marketing and promotion**

In February 2004, the Group received a subpoena from the US Attorney's office in Colorado regarding the Group's sales and promotional practices relating to nine of its largest selling products for the period from January 1997 to the present. In particular the government has inquired about alleged promotion of these drugs for off-label uses as well as Group sponsored continuing medical education programmes, other speaker events, special issue boards, advisory boards, speaker training programmes, clinical studies, and related grants, fees, travel and entertainment. Although the original subpoena issued from the US Attorney's office in Colorado, the scope of the inquiry is nationwide. The Group is co-operating with the investigation and providing the requested information. The Group had earlier responded to an October 2002 letter from the FDA's Division of Drug Marketing, Advertising and Communication requesting information on the Group's alleged promotion of *Wellbutrin SR* for off-label use.

In June 2005, the Group and other pharmaceutical manufacturers received a letter from the US Senate Finance Committee in which the Committee expressed concern that educational grants were being improperly used to promote drug products and requesting that each company provide detailed information and documents about its use of educational grants. In January 2006, the Group and the same manufacturers received a second letter from the Committee asking for additional information on the Group's internal grant approval process, grants to medical/physician/professional organisations, academic institutions or state agencies to support journal articles and other publications and grants to patient education or advocacy groups. The Group is co-operating in the Committee's investigation and providing the requested information.

In February 2003, the Verona Public Prosecutor commenced a criminal investigation into GSK's sales and marketing practices in Italy. Specific areas of investigation include medical education programmes, clinical studies and congresses as well as the interaction between GSK representatives and physicians. The US Securities and Exchange Commission (SEC) staff has initiated an investigation into the allegations. The Group is co-operating with both of these investigations.

In February 2006, the Group received a subpoena from the SEC in respect of the Group's participation in the United Nations Oil for Food Programme. The Group is co-operating with the SEC and providing documents responsive to the subpoena. The US Department of Justice is also investigating this matter.

Average wholesale price

GSK has responded to subpoenas from the Office of the Inspector General of the US Department of Health and Human Services (HHS), the US Department of Justice and the states of Texas and California in connection with allegations that pharmaceutical companies, including GSK, have violated federal fraud and abuse laws such as the Federal False Claims Act (and, with respect to Texas and California, comparable state laws) as a result of the way 'average wholesale price' (AWP) was determined and reported for certain drugs and the way the Medicare and Medicaid programmes reimburse for those drugs. In September 2005, the Group reached a civil settlement with the US Department of Justice, the US Attorney for the District of Massachusetts and the Office of the Inspector General for HHS (the "DOJ Settlement"). The Group agreed to pay the government a civil settlement of \$149 million, which included settlement amounts for each of the states for the claims being settled. As part of the settlement the corporate integrity agreement to which the Group is a party was amended to address issues raised in the course of the government investigation.

Subsequent to the initial subpoenas, a number of states through their respective attorneys general and most of the counties in New York state filed civil lawsuits in state and federal courts against GSK and many other drug companies. The actions claim, on behalf of the states as payers (and in some cases on behalf of in-state patients as consumers), damages and restitution due to AWP-based price reporting for pharmaceutical products covered by the states' Medicaid programmes (and in some cases by other governmental programmes). In addition, private payer class action lawsuits were filed against GSK in multiple federal district and state courts. All the federal cases were consolidated in a MDL proceeding in the US District Court for the District of Massachusetts.

In August 2005, the judge in that MDL proceeding granted in part and denied in part the private-payer plaintiffs' motion for class certification, thereby narrowing the scope of the class claims. In August 2006 the Group reached civil settlements to resolve the class action litigation and certain of the state attorney general claims. The Group agreed to a nationwide settlement (subject to court approval) of \$70 million to resolve these claims. The Group separately resolved potential AWP claims by state Medicaid programmes in more than two-thirds of the states through the procedures established by the DOJ Settlement, and also fully resolved AWP lawsuits filed or threatened by a number of state attorneys general. Litigation concerning AWP issues is continuing with a group of other state attorneys general as well as with New York counties.

Nominal pricing

The Group responded to two letter requests from the US Senate Committee on Finance, dated April 2004 and February 2005, for documents and information relating to the nominal price exception to the best price reporting requirements under the Medicaid Drug Rebate Programme. There has been no further activity in connection with this inquiry by the Committee as to the Group since September 2005. In May 2004, the Group was advised by the US Department of Justice that they are investigating certain of the Group's nominal pricing arrangements to determine whether those arrangements qualify under the exception to the best price reporting requirements or violate civil statutes or laws. The Group is co-operating in that investigation and has provided documents and information to the Department of Justice regarding nominal pricing arrangements for a number of the Group's products.

Notes to the financial statements

continued

43 Legal proceedings continued

Paxil/Seroxat

Following announcement of the New York State Attorney General's office about the state's lawsuit, subsequently settled in August 2004, alleging failure to disclose data on the use of *Paxil* in children and adolescents, similar cases, some of which purport to be class actions, have been filed in state and federal and Canadian courts by private plaintiffs seeking to recover amounts paid for *Paxil* purchased for use by patients under age 18. The Group reached a class settlement agreement in an Illinois state court action that would include all persons in the USA who bought *Paxil* for someone under age 18. The Group denies any liability. The agreement relates only to the cost of purchasing *Paxil* for use by paediatric patients and does not include any personal injury claims. The settlement received preliminary approval by a judge in Madison County, Illinois in October 2006. The final fairness hearing on the settlement is scheduled for 25th April 2007.

In the UK an investigation remains pending by the UK Medicines and Healthcare products Regulatory Agency (MHRA) to determine whether the Group has complied with its pharmacovigilance obligations in reporting data from clinical trials for *Seroxat/Paxil* in children and adolescents.

Cidra, Puerto Rico manufacturing site

Following FDA inspections in October 2003 and November 2004 which resulted in observations of possible deficiencies in manufacturing practices at the Group's manufacturing facility in Cidra, Puerto Rico, in March 2005 the FDA halted distribution of supplies of *Paxil CR* and *Avandamet* due to manufacturing issues. The FDA observations related to certain aspects of production controls, process validation and laboratory investigations.

The Cidra site is engaged in tableting and packaging for a range of GlaxoSmithKline products – primarily for the US market – including *Paxil*, *Paxil CR*, *Coreg*, *Avandia*, and *Avandamet*. In April 2005 the Group reached agreement with the FDA on a Consent Decree. The Consent Decree provides for an independent expert to review manufacturing processes at the site for compliance with FDA Good Manufacturing Practice (GMP) requirements. As provided in the Consent Decree, the Group provided a report to the FDA on the deficiencies identified in this review, setting out a corrective plan and timetable for completion. The Group remains fully committed to working cooperatively with the FDA to address any issues in a timely fashion. The Group has resumed manufacture of products at the site. In June 2006, the FDA confirmed that the status for the site had been upgraded to 'voluntary action indicated,' which means that the FDA deems the site acceptable for the export of products and for routine manufacturing operations.

No financial penalties have been imposed under the Consent Decree. The Consent Decree allows for potential future penalties up to a maximum of \$10 million a year if the Group fails to meet the terms of the Consent Decree.

In April 2005, the Group received a subpoena from the US Attorney's Office in Boston requesting production of records regarding manufacturing at the Cidra site covering the same type of information as that collected by the US government in Puerto Rico in 2003. The Group is co-operating with the US Attorney's Office and producing the records responsive to the subpoena. The Group is also named in two purported consumer fraud class action lawsuits – one filed in California state court and the other in the US District Court for the District of Puerto Rico – alleging that *Paxil CR* and/or *Paxil Oral Suspension* were not manufactured according to GMP. Plaintiffs seek economic, statutory and punitive damages, along with a request for injunctive relief. There has not yet been any determination whether either case will be permitted to proceed as a class action.

Anti-trust

Paxil/Seroxat

In the paroxetine patent infringement actions brought by the Group as described under 'Intellectual property' above, Apotex, Alphapharm, BASF and Sumika have filed anti-trust and unfair competition counterclaims against the Group in the US District Court for the Eastern District of Pennsylvania based on allegations that the Group monopolised a 'market' for *Paxil* by bringing allegedly sham patent litigation and allegedly abusing the regulatory procedures for the listing of patents in the FDA Orange Book. Whilst the Apotex matter remains in the discovery stage, the Alphapharm and BASF matters have been resolved and a settlement agreement in principle has been reached with Sumika.

In November 2000, the US Federal Trade Commission (FTC) staff advised the Group that they were conducting a non-public investigation to determine whether the Group was violating Section 5 of the Federal Trade Commission Act by 'monopolising or attempting to monopolise' the market for paroxetine hydrochloride by preventing generic competition to *Paxil* and requested the Group to submit certain information in connection with that investigation. In October 2003, the FTC closed its investigation on the basis of its finding that no further action was warranted.

Following public reference to the FTC investigation regarding *Paxil*, a number of governmental and private civil actions and claims were initiated in the USA. All have been resolved with the exception of a private indirect purchaser opt-out lawsuit brought in Minnesota state court. That matter is in the discovery phase. Additionally, class actions have been filed in provincial courts in Canada on behalf of direct and indirect purchasers. Those cases are in their early stages.

43 Legal proceedings continued

In October 2005, the Competition Directorate of the European Commission initiated an inspection concerning allegations that the Group has abused a dominant position in the marketplace concerning enforcement of its intellectual property rights, litigation surrounding regulatory approvals and marketing of *Seroxat* in Europe. In October 2006, the Commission made a formal request for further information. The Group continues to co-operate fully with the Commission.

Canadian importation

The Group has been named in seven purported class action lawsuits along with eight other pharmaceutical companies. Following the Group's actions in 2003 to reduce illegal importation of prescription drugs from Canada, the lawsuits alleged that the companies entered into an unlawful conspiracy to prevent Canadian pharmacies from selling their products to US customers. Those lawsuits were consolidated into one action before the US District Court for the District of Minnesota. The Group's motion to dismiss the consolidated action was granted by the court and affirmed by the US Circuit Court of Appeals for the Eighth Circuit in November 2006.

In relation to the same matter, the Minnesota state attorney general has filed a civil investigative demand and, subsequently, a complaint alleging that the Group has violated state anti-trust and commercial laws. That case is still in the discovery phase.

The Group has also been named as a defendant, along with thirteen other drug companies, in a state court action in California, in which the plaintiffs, independent pharmacies, allege that the defendants unlawfully conspired to keep prices artificially high in the USA to the detriment of the plaintiffs. In December 2006, the trial judge granted the Group's motion for summary judgement. Plaintiffs have filed an appeal with the California Court of Appeals.

Wellbutrin SR

In December 2004, and January and February 2005, lawsuits, several of which purported to be class actions, were filed in the US District Court for the Eastern District of Pennsylvania against the Group on behalf of direct and indirect purchasers of *Wellbutrin SR*. The complaints allege violations of US anti-trust laws through sham litigation and fraud on the patent office by the Group in obtaining and enforcing patents covering *Wellbutrin SR*. The complaints follow the introduction of generic competition to *Wellbutrin SR* in April 2004 after district and appellate court rulings that a generic manufacturer did not infringe the Group's patents. The parties are involved in discovery.

Secondary wholesaler

In July 2006, RxUSA Wholesale, Inc., a 'secondary wholesaler', filed suit against the Group and many other pharmaceutical manufacturers and wholesalers in the US District Court for the Eastern District of New York. The complaint alleges that the defendants engaged in a conspiracy to refuse to supply pharmaceutical products to RxUSA in violation of federal and state anti-trust laws. The Group's motion to dismiss the complaint is pending.

Commercial and corporate**Relenza**

In May 2004, Biota Holdings Limited filed a complaint in the Victorian Supreme Court in Australia alleging that the Group had failed to fulfil its development, promotion and production obligations for zanamivir (*Relenza*) under the terms of the licence agreement between the Group and Biota. Biota is seeking substantial cash damages. The Group believes that it has adhered to its obligations under the licence agreement. The parties are involved in extensive discovery.

Securities class action

In September 2005, attorneys representing a purported class of purchasers of GlaxoSmithKline shares and American Depositary Shares (ADSs) filed a second amended securities class action complaint against the Group in the US District Court for the Southern District of New York alleging that the Group violated US securities laws through failure to disclose unfavourable clinical data from studies on *Paxil*, misrepresentation of the remaining patent protection for *Paxil* and *Augmentin* and violation of the Federal False Claims Act on the basis of the Group's recent AWP settlement with the government. In October 2006, the judge entered an order dismissing the complaint. Plaintiffs have filed an appeal with the US Court of Appeals for the Second Circuit.

Overtime claims

In December 2006, two purported class actions were filed in the US District Courts for the Central and Southern Districts of California against the Group on behalf of all the Group's US pharmaceutical sales representatives. The actions allege that those representatives are not 'exempt' employees under the US Fair Labor Standards Act and consequently entitled to overtime pay. The suits seek double damages for all overtime allegedly worked by the Group's sales representatives over a three-year period together with attorneys' fees. Similar actions have been filed against other pharmaceutical companies. The cases are in their early stages.

Environmental matters

GSK has been notified of its potential responsibility relating to past operations and its past waste disposal practices at certain sites, primarily in the USA. Some of these matters are the subject of litigation, including proceedings initiated by the US federal or state governments for waste disposal site remediation costs and tort actions brought by private parties.

GSK has been advised that it may be a responsible party at approximately 29 sites, of which 14 appear on the National Priority List created by the Comprehensive Environmental Response Compensation and Liability Act (Superfund).

Notes to the financial statements

continued

43 Legal proceedings continued

These proceedings seek to require the operators of hazardous waste facilities, transporters of waste to the sites and generators of hazardous waste disposed of at the sites to clean up the sites or to reimburse the government for cleanup costs. In most instances, GSK is involved as an alleged generator of hazardous waste although there are a few sites where GSK is involved as a current or former operator of the facility. Although Superfund provides that the defendants are jointly and severally liable for cleanup costs, these proceedings are frequently resolved on the basis of the nature and quantity of waste disposed of at the site by the generator. GSK's proportionate liability for cleanup costs has been substantially determined for about 20 of the sites referred to above.

GSK's potential liability varies greatly from site to site. While the cost of investigation, study and remediation at such sites could, over time, be substantial, GSK routinely accrues amounts related to its share of the liability for such matters.

Tax matters

Pending tax matters are described in Note 12.

Directors' statements of responsibility

Directors' statement of responsibility in relation to the company's financial statements

The Directors are:

- responsible for ensuring the maintenance of proper accounting records, which disclose with reasonable accuracy the financial position of the company at any time and from which financial statements can be prepared to comply with the Companies Act 1985
- required by law to prepare financial statements for each financial period which give a true and fair view of the state of affairs of the company as at the end of the financial period and of the profit or loss for that period
- responsible also for ensuring the operation of systems of internal control and for taking reasonable steps to safeguard the assets of the company and for preventing and detecting fraud and other irregularities.

The balance sheet for the year ended 31st December 2006, and supporting notes are set out on pages 167 to 170 of this report.

The Directors confirm that suitable accounting policies have been consistently applied in the preparation of the financial statements, supported by reasonable and prudent judgements and estimates as necessary; applicable accounting standards have been followed, and the financial statements have been prepared on the going concern basis.

The responsibilities of the auditors in relation to the financial statements are set out in the Independent Auditors' report (page 166).

The Annual Report 2006 is published in hard-copy printed form and made available on the website. The Directors are responsible for the maintenance and integrity of the Annual Report on the website in accordance with UK legislation governing the preparation and dissemination of financial statements. Access to the website is available from outside the UK, where comparable legislation may be different.

Disclosure of information to auditors

The Directors, in office at the date of this Report, have each confirmed that:

- so far as they are aware, there is no relevant audit information of which the company's auditors are unaware; and
- each Director has taken all the steps that he/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 234 ZA of the Companies Act 1985.

Directors' remuneration

The Remuneration Report on pages 65 to 82 sets out the remuneration policies operated by GlaxoSmithKline and disclosures on Directors' remuneration and other disclosable information relating to Directors and officers and their interests. It has been prepared in accordance with the Companies Act 1985 and complies with Section B of the Combined Code on Corporate Governance.

Going concern basis

After making enquiries, the Directors have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

The Combined Code

The Board considers that GlaxoSmithKline plc applies the principles of the Combined Code on Corporate Governance of the Financial Reporting Council, as described under 'Corporate governance' on pages 53 to 63, and has complied with its provisions except as described on page 62.

As required by the Listing Rules of the Financial Services Authority, the auditors have considered the Directors' statement of compliance in relation to those points of the Combined Code which are specified for their review.

Sir Christopher Gent

Chairman

28th February 2007

Independent Auditors' report

to the members of GlaxoSmithKline plc

We have audited the parent company financial statements of GlaxoSmithKline plc for the year ended 31st December 2006 which comprise the Balance Sheet and the related notes. These parent company financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

We have reported separately on the Group financial statements of GlaxoSmithKline for the year ended 31st December 2006.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report, the Directors' Remuneration Report and the parent company financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the parent company financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the parent company financial statements give a true and fair view and whether the parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Report of the Directors is consistent with the parent company financial statements.

In addition we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited parent company financial statements. The other information comprises only the Financial summary, the Joint statement by the Chairman and Chief Executive, Financial trends and ratios, Business review, the Corporate governance statement and unaudited parts of the Remuneration report. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the parent company financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the parent company financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the parent company financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the parent company financial statements and the part of the Directors' Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the parent company financial statements and the part of the Directors' Remuneration Report to be audited.

Opinion

In our opinion:

- the parent company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31st December 2006;
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Report of the Directors is consistent with the parent company financial statements.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London
28th February 2007

Company balance sheet – UK GAAP

at 31st December 2006

	Notes	2006 £m	2005 (restated) £m
Investment in subsidiary companies		19,466	18,750
Fixed assets	E	19,466	18,750
Debtors	F	273	237
Cash at bank		7	5
Current assets		280	242
Creditors: amounts due within one year	G	(10,210)	(8,885)
Net current liabilities		(9,930)	(8,643)
Net assets		9,536	10,107
Capital and reserves			
Called up share capital	H	1,498	1,491
Share premium account	H	858	549
Other reserves	I	1,008	902
Profit and loss account	I	6,172	7,165
Equity shareholders' funds		9,536	10,107

Approved by the Board on 28th February 2007

Sir Christopher Gent
Chairman

Notes to the company balance sheet – UK GAAP

A Presentation of the financial statements**Description of business**

GlaxoSmithKline plc is the parent company of GSK, a major global healthcare group which is engaged in the creation and discovery, development, manufacture and marketing of pharmaceutical products, including vaccines, over-the-counter (OTC) medicines and health-related consumer products.

Preparation of financial statements

The financial statements are drawn up in accordance with UK generally accepted accounting principles (UK GAAP) and with UK accounting presentation as at 31st December 2006, with comparative figures as at 31st December 2005.

As permitted by s.230 of the Companies Act 1985, the profit and loss account of the company is not presented in this Annual Report.

Accounting convention and standards

The balance sheet has been prepared using the historical cost convention and complies with applicable UK accounting standards.

Accounting principles and policies

The preparation of the balance sheet in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the balance sheet. Actual amounts could differ from those estimates.

The balance sheet has been prepared in accordance with the company's accounting policies approved by the Board and described in Note B.

B Accounting policies**Foreign currency transactions**

Foreign currency transactions are recorded at the exchange rate ruling on the date of transaction, or at the forward rate if hedged by a forward exchange contract. Foreign currency assets and liabilities are translated at rates of exchange ruling at the balance sheet date, or at the forward rate.

Dividends paid and received

Dividends paid and received are included in the accounts in the period in which the related dividends are actually paid or received.

Expenditure

Expenditure is recognised in respect of goods and services received when supplied in accordance with contractual terms. Provision is made when an obligation exists for a future liability in respect of a past event and where the amount of the obligation can be reliably estimated.

Investments in subsidiary companies

Investments in subsidiary companies are held at cost less any provision for permanent diminution in value.

Impairment of investments

The carrying value of investments are reviewed for impairment when there is an indication that the investment might be impaired. Any provision resulting from an impairment review is charged to the income statement in the year concerned.

Share based payments

The issuance by the company to its subsidiaries of a grant over the company's options, represents additional capital contributions by the company in its subsidiaries. An additional investment in subsidiaries results in a corresponding increase in shareholders' equity. The additional capital contribution is based on the fair value of the grant issued allocated over the underlying grant's vesting period.

Taxation

Current tax is provided at the amounts expected to be paid applying tax rates that have been enacted or substantially enacted by the balance sheet date.

The company accounts for taxation which is deferred or accelerated by reason of timing differences which have originated but not reversed by the balance sheet date. Deferred tax assets are only recognised to the extent that they are considered recoverable against future taxable profits.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse. Deferred tax liabilities and assets are not discounted.

Financial guarantees

Financial guarantees issued between the company and its subsidiaries are held at fair value and amortised over the life of the guarantee.

C New accounting policies

The ASB issued an amendment to FRS 26 'Financial Instruments: Measurement' in April 2006. This has been adopted by the company in 2006. The amended standard implements the sections of IAS 39 relating to recognition and derecognition. The adoption of this amended standard has the effect of recognising the fair value of financial guarantees issued by the company, and as a result the comparative figures of the company have been restated by increasing both investment in subsidiary companies and other creditors by £23 million. There is no impact on profits previously reported.

D Operating profit

A fee of £10,700 (2005 – £10,700) relating to the audit of the company has been charged in operating profit.

Notes to the company balance sheet – UK GAAP

continued

E Fixed assets

	2006 £m	2005 (restated) £m
Shares in GlaxoSmithKline Finance plc	–	17,888
Shares in GlaxoSmithKline Services Unlimited	613	–
Shares in GlaxoSmithKline Holdings (One) Limited	18	18
Shares in GlaxoSmithKline Holdings Limited	17,888	–
	18,519	17,906
Capital contribution relating to share based payments and financial guarantees	947	844
	19,466	18,750

During the year the company formed a new subsidiary, GlaxoSmithKline Holdings Limited, and sold its entire shareholding in GlaxoSmithKline Finance plc to it. GlaxoSmithKline Holdings Limited issued new shares to the company as consideration. The company also paid £613 million in consideration for the issue of new shares from GlaxoSmithKline Services Unlimited.

F Debtors

	2006 £m	2005 £m
Amounts due within one year:		
Corporate tax	271	127
Amounts owed by Group undertakings	2	110
	273	237

G Creditors

	2006 £m	2005 (restated) £m
Amounts due within one year:		
Dividends payable	4	4
Amounts owed to Group undertakings	10,185	8,857
Other creditors	21	24
	10,210	8,885

H Share capital and share premium account

	Ordinary shares of 25p each Number	£m	Share premium £m
Share capital authorised			
At 31st December 2005	10,000,000,000	2,500	
At 31st December 2006	10,000,000,000	2,500	
Share capital issued and fully paid			
At 1st January 2005	5,937,688,831	1,484	304
Issued under share option schemes	25,162,425	7	245
At 31st December 2005	5,962,851,256	1,491	549
Issued under share option schemes	28,750,592	7	309
At 31st December 2006	5,991,601,848	1,498	858
	31st December 2006		31st December 2005
Number ('000) of shares issuable under outstanding options	222,163		221,293
Number ('000) of unissued shares not under option	3,786,235		3,815,856

At 31st December 2006, of the issued share capital, 153,451,642 shares were held in the ESOP Trust, 235,482,678 shares were held as Treasury shares and 5,602,667,528 shares were in free issue. All issued shares are fully paid. The nominal, carrying and market values of the shares held in the ESOP Trust are disclosed in Note 40.

Notes to the company balance sheet – UK GAAP

continued

I Reserves

	Other reserves £m	Profit and loss account £m	Total £m
At 1st January 2005	767	9,476	10,243
Profit attributable to shareholders	–	1,079	1,079
Dividends to shareholders	–	(2,390)	(2,390)
Ordinary shares purchased and held as Treasury shares	–	(1,000)	(1,000)
Capital contribution relating to share based payments	135	–	135
At 31st December 2005	902	7,165	8,067
Profit attributable to shareholders	–	2,953	2,953
Dividends to shareholders	–	(2,598)	(2,598)
Ordinary shares purchased and held as Treasury shares	–	(1,348)	(1,348)
Capital contribution relating to share based payments	106	–	106
At 31st December 2006	1,008	6,172	7,180

The profit of GlaxoSmithKline plc for the year was £2,953 million (2005 – £1,079 million), which after dividends of £2,598 million (2005 – £2,390 million), gave a retained profit of £355 million (2005 – loss £1,311 million). After the cost of shares purchased and held as Treasury shares of £1,348 million (2005 – £1,000 million), the profit and loss account reserve at 31st December 2006 stood at £6,172 million (2005 – £7,165 million), of which £4,096 million is unrealised (2005 – £4,096 million).

Investor information

This section includes the financial record presenting historical information analysed in accordance with current reporting practice. The transition date to IFRS for GSK was 1st January 2003. Therefore, the 2006, 2005, 2004 and 2003 information included in the Five year record is in accordance with IFRS. The 2002 information is in accordance with UK GAAP.

To provide a link between IFRS and UK GAAP, 2003 information is presented also under UK GAAP. The accounting policies used in the preparation of the UK GAAP information are disclosed in the 2004 Annual Report. Information prepared under IFRS is not directly comparable with information prepared under UK GAAP.

The Five year record also presents information in accordance with US GAAP.

This section also discusses shareholder return, in the form of dividends and share price movements, and provides other information for shareholders.

Financial record	
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Five year record	178
Shareholder information	182
Taxation information for shareholders	186

Financial record

Quarterly trend

An unaudited analysis is provided by quarter of the Group results and pharmaceutical sales by therapeutic area in Sterling for the financial year 2006.

Income statement

	12 months 2006			Q4 2006		
	£m	CER %	£%	£m	CER %	£%
Turnover – Pharmaceuticals	20,078	9	8	5,136	8	1
– Consumer Healthcare	3,147	6	5	823	9	3
Total turnover	23,225	9	7	5,959	9	1
Cost of sales	(5,010)	6	5	(1,445)	15	11
Selling, general and administrative	(7,257)	–	–	(1,934)	–	(5)
Research and development	(3,457)	11	10	(980)	6	1
Other operating income	307			100		
Operating profit	7,808	17	14	1,700	19	4
Finance income	287			83		
Finance costs	(352)			(86)		
Share of after tax profits of associates and joint ventures	56			13		
Profit before taxation	7,799	19	16	1,710	22	6
Taxation	(2,301)			(505)		
<i>Tax rate %</i>	<i>29.5%</i>			<i>29.5%</i>		
Profit after taxation for the period	5,498	17	14	1,205	20	5
Profit attributable to minority interests	109			24		
Profit attributable to shareholders	5,389			1,181		
Basic earnings per share (pence)	95.5p	19	16	21.0p	22	6
Diluted earnings per share (pence)	94.5p			20.8p		

Q3 2006			Q2 2006			Q1 2006		
£m	CER %	£%	£m	CER %	£%	£m	CER %	£%
4,876	7	4	5,021	10	11	5,045	10	16
766	4	1	790	5	7	768	6	10
5,642	7	3	5,811	9	11	5,813	10	15
(1,222)	5	3	(1,209)	3	5	(1,134)	(2)	1
(1,617)	(10)	(14)	(1,883)	8	12	(1,823)	5	11
(871)	11	8	(853)	20	22	(753)	10	14
91			45			71		
2,023	19	13	1,911	13	12	2,174	15	24
64			67			73		
(81)			(93)			(92)		
16			12			15		
2,022	21	15	1,897	15	14	2,170	17	27
(596)			(560)			(640)		
29.5%			29.5%			29.5%		
1,426	19	14	1,337	14	12	1,530	16	25
35			22			28		
1,391			1,315			1,502		
24.7p	21	16	23.3p	15	14	26.5p	17	26
24.4p			23.0p			26.3p		

Financial record

continued

Pharmaceutical turnover – total Group

	Q4 2006			Q3 2006			Q2 2006			Q1 2006		
	£m	CER %	£%	£m	CER %	£%	£m	CER %	£%	£m	CER %	£%
Respiratory	1,269	(3)	(10)	1,185	(1)	(4)	1,232	–	1	1,309	4	9
<i>Seretide/Advair</i>	862	9	1	813	14	10	822	12	13	816	12	18
<i>Flixotide/Flovent</i>	172	7	(1)	145	(1)	(4)	164	2	3	178	10	16
<i>Serevent</i>	74	(9)	(15)	69	(10)	(13)	74	(13)	(13)	74	(9)	(6)
<i>Flixonase/Flonase</i>	48	(69)	(72)	64	(59)	(61)	68	(53)	(54)	131	(27)	(23)
Central Nervous System	915	13	3	913	18	13	918	18	19	896	11	18
<i>Seroxat/Paxil</i>	163	11	3	137	4	(3)	159	5	4	161	(4)	(1)
<i>Paxil IR</i>	113	–	(7)	103	(8)	(13)	122	(1)	(3)	110	(11)	(10)
<i>Paxil CR</i>	50	50	39	34	61	48	37	33	37	51	15	24
<i>Wellbutrin</i>	212	9	(2)	234	27	22	237	40	42	217	22	33
<i>Wellbutrin IR, SR</i>	25	13	4	26	17	13	27	>100	>100	24	(31)	(25)
<i>Wellbutrin XL</i>	187	9	(3)	208	28	23	210	34	36	193	35	47
<i>Imigran/Imitrex</i>	174	2	(7)	180	4	–	175	7	8	182	2	9
<i>Lamictal</i>	257	23	13	257	27	22	245	12	13	237	14	22
<i>Requip</i>	76	62	52	70	71	67	64	85	88	58	83	93
Anti-virals	706	9	1	703	9	6	719	12	13	699	10	16
HIV	360	(5)	(11)	363	(6)	(9)	393	1	2	399	4	10
<i>Combivir</i>	119	(14)	(20)	125	(12)	(15)	141	(6)	(5)	143	(3)	2
<i>Trizivir</i>	61	(14)	(21)	63	(16)	(18)	72	(5)	(4)	72	(7)	(3)
<i>Epivir</i>	43	(24)	(31)	46	(25)	(29)	53	(25)	(22)	60	(12)	(9)
<i>Ziagen</i>	28	(12)	(18)	28	(12)	(15)	29	(19)	(19)	32	(9)	(3)
<i>Agenerase, Lexiva</i>	34	12	3	32	3	3	32	23	23	33	41	50
<i>Epzicom/Kivexa</i>	69	66	57	63	88	85	58	>100	>100	51	>100	>100
Herpes	242	18	8	242	21	15	245	25	26	236	13	20
<i>Valtrex</i>	212	23	12	215	26	20	214	30	32	204	16	24
<i>Zovirax</i>	30	(9)	(12)	27	(6)	(13)	31	(3)	(6)	32	(6)	(3)
<i>Zeffix</i>	42	5	–	42	16	14	40	5	8	38	24	31
<i>Relenza</i>	37	>100	>100	30	–	–	17	>100	>100	7	>100	>100
Metabolic	474	34	22	438	16	11	529	32	35	434	26	36
<i>Avandia</i>	324	25	12	323	13	8	408	23	26	344	30	42
<i>Avandamet</i>	68	54	48	44	(21)	(23)	64	>100	>100	28	(39)	(36)
<i>Avandaryl</i>	14	–	–	11	–	–	5	–	–	12	–	–
<i>Bonviva/Boniva</i>	34	>100	>100	27	>100	>100	19	>100	>100	15	–	–
Vaccines	527	31	25	412	5	3	387	17	20	366	44	48
<i>Hepatitis</i>	128	19	14	114	(2)	(5)	121	3	4	116	18	23
<i>Infanrix, Pediarix</i>	136	29	21	122	6	3	129	38	40	124	54	59
<i>Boostrix</i>	18	73	64	18	64	64	14	>100	>100	10	>100	>100
Cardiovascular and urogenital	421	25	15	406	23	18	383	21	23	426	29	37
<i>Coreg</i>	199	39	25	195	32	27	160	29	28	225	53	67
<i>Levitra</i>	12	30	20	11	22	22	9	(18)	(18)	11	–	10
<i>Avodart</i>	61	67	56	57	61	58	51	79	82	47	73	81
<i>Arixtra</i>	21	>100	>100	13	100	86	13	>100	>100	11	>100	>100
<i>Fraxiparine</i>	53	(2)	(4)	49	2	–	56	–	2	51	(4)	(2)
Anti-bacterials	354	(8)	(13)	311	(8)	(11)	326	(8)	(6)	378	(12)	(9)
<i>Augmentin</i>	145	(11)	(15)	121	(15)	(19)	134	(15)	(13)	170	(14)	(11)
<i>Zinnat/Ceftin</i>	42	(19)	(22)	35	(10)	(15)	37	(10)	(8)	50	(23)	(19)
Oncology and emesis	213	(11)	(21)	279	11	6	289	15	17	288	14	23
<i>Zofran</i>	165	(19)	(28)	223	8	4	229	11	12	230	13	22
<i>Hycamtin</i>	28	20	12	28	12	8	28	22	22	29	8	16
Other	257	2	(4)	229	(7)	(10)	238	(9)	(10)	249	(6)	(1)
<i>Zantac</i>	55	(5)	(14)	51	(11)	(16)	61	2	2	65	7	10
Total	5,136	8	1	4,876	7	4	5,021	10	11	5,045	10	16

Pharmaceutical turnover includes co-promotion income.

Financial record

continued

Five year record

A record of financial performance is provided analysed in accordance with current reporting practice. The transition date to IFRS for GlaxoSmithKline was 1st January 2003. Therefore, the 2006, 2005, 2004 and 2003 information included in the Five year record is in accordance with IFRS as adopted for use in the European Union. For GSK there are no differences between IFRS as adopted for use in the European Union and full IFRS as published by the International Accounting Standards Board. The 2002 information is in accordance with UK GAAP.

To provide a link between IFRS and UK GAAP, 2003 information is also presented under UK GAAP. The accounting policies used in the preparation of the UK GAAP information are disclosed in the 2004 Annual Report. Information prepared under IFRS is not directly comparable with information prepared under UK GAAP.

The Five year record also presents information in accordance with US GAAP.

Turnover by business segment – IFRS

	2006 £m	2005 £m	2004 £m	2003 £m
Pharmaceuticals	20,078	18,661	17,100	18,114
Consumer Healthcare	3,147	2,999	2,886	2,956
	23,225	21,660	19,986	21,070

Turnover by business segment – UK GAAP

	2003 £m	2002 £m
Pharmaceuticals	18,181	17,995
Consumer Healthcare	3,260	3,217
	21,441	21,212

Pharmaceutical turnover by therapeutic area – IFRS

	2006 £m	2005 £m	2004 £m	2003 £m
Respiratory	4,995	5,054	4,394	4,390
Central nervous system	3,642	3,219	3,462	4,446
Anti-virals	2,827	2,598	2,359	2,345
Metabolic	1,875	1,495	1,251	1,077
Vaccines	1,692	1,389	1,194	1,121
Cardiovascular and urogenital	1,636	1,331	932	770
Anti-bacterials	1,369	1,519	1,547	1,800
Oncology and emesis	1,069	1,016	934	1,000
Other	973	1,040	1,027	1,165
	20,078	18,661	17,100	18,114

Pharmaceutical turnover by therapeutic area – UK GAAP

	2003 £m	2002 £m
Respiratory	4,417	3,987
Central nervous system	4,455	4,511
Anti-virals	2,349	2,299
Metabolic	1,079	960
Vaccines	1,123	1,080
Cardiovascular and urogenital	771	661
Anti-bacterials	1,815	2,210
Oncology and emesis	1,001	977
Others	1,171	1,310
	18,181	17,995

Pharmaceutical turnover by geographic area – IFRS

	2006 £m	2005 £m	2004 £m	2003 £m
USA	10,353	9,106	8,425	9,410
Europe	5,547	5,537	5,084	5,050
International:				
Asia Pacific	1,377	1,324	1,161	1,138
Japan	860	854	769	751
Middle East, Africa	744	746	669	693
Latin America	714	651	581	598
Canada	483	443	411	474
International	4,178	4,018	3,591	3,654
	20,078	18,661	17,100	18,114

Pharmaceutical turnover by geographic area – UK GAAP

	2003 £m	2002 £m
USA	9,410	9,797
Europe	5,114	4,701
International:		
Asia Pacific	1,140	1,100
Japan	753	712
Middle East, Africa	693	652
Latin America	597	606
Canada	474	427
International	3,657	3,497
	18,181	17,995

Pharmaceutical turnover in 2006, 2005, 2004 and 2003 includes co-promotion income.

Consumer healthcare turnover – IFRS

	2006 £m	2005 £m	2004 £m	2003 £m
OTC medicines	1,496	1,437	1,400	1,472
Oral care	993	943	913	915
Nutritional healthcare	658	619	573	569
	3,147	2,999	2,886	2,956

Consumer healthcare turnover – UK GAAP

	2003 £m	2002 £m
OTC medicines	1,556	1,586
Oral care	1,082	1,052
Nutritional healthcare	622	579
	3,260	3,217

Financial results – IFRS

	2006 £m	2005 £m	2004 £m	2003 £m
Turnover	23,225	21,660	19,986	21,070
Operating profit	7,808	6,874	5,756	6,050
Profit before taxation	7,799	6,732	5,779	5,954
Profit after taxation	5,498	4,816	4,022	4,308
Basic earnings per share (pence)	95.5p	82.6p	68.1p	72.3p
Diluted earnings per share (pence)	94.5p	82.0p	68.0p	72.1p
Weighted average number of shares in issue:				
Basic	5,643	5,674	5,736	5,806
Diluted	5,700	5,720	5,748	5,824
Return on capital employed (%)	90.6	99.7	100.2	116.6

Financial results – UK GAAP

	2003 £m	2002 £m
Turnover	21,441	21,212
Operating profit	6,376	5,569
Profit before taxation	6,313	5,524
Profit after taxation	4,584	4,060
Basic earnings per share (pence)	77.1p	66.5p
Diluted earnings per share (pence)	76.9p	66.3p
Weighted average number of shares in issue:		
Basic	5,806	5,912
Diluted	5,824	5,934
Return on capital employed (%)	120.8	110.6

Return on capital employed is calculated as statutory profit before taxation as a percentage of average capital employed over the year.

Financial record

continued

Amounts in accordance with US GAAP	2006 £m	2005 £m	2004 £m	2003 £m	2002 £m
Turnover	23,225	21,660	19,986	21,117	21,212
Net income	4,465	3,336	2,732	2,420	413
Basic net income per share (pence)	79.1p	58.8p	47.6p	41.7p	7.0p
Diluted net income per share (pence)	78.4p	58.3p	47.5p	41.6p	7.0p

The information presented in accordance with US GAAP is derived from financial information prepared under IFRS, as adopted for use in the European Union, for 2003-2006 and from UK GAAP for 2002.

Balance sheet – IFRS

	2006 £m	2005 £m	2004 £m	2003 £m
Non-current assets	14,561	14,021	12,164	11,622
Current assets	10,992	13,177	10,780	10,298
Total assets	25,553	27,198	22,944	21,920
Current liabilities	(7,265)	(9,511)	(8,564)	(8,314)
Non-current liabilities	(8,640)	(10,117)	(8,443)	(8,008)
Total liabilities	(15,905)	(19,628)	(17,007)	(16,322)
Net assets	9,648	7,570	5,937	5,598
Equity				
Shareholders' equity	9,386	7,311	5,724	4,917
Minority interests	262	259	213	681
	9,648	7,570	5,937	5,598

Balance sheet – UK GAAP

		2003 £m	2002 £m
Fixed assets		8,575	8,752
Current assets		12,625	10,749
Total assets		21,200	19,501
Current liabilities		(8,471)	(8,724)
Non-current liabilities		(6,925)	(6,130)
Total liabilities		(15,396)	(14,854)
Net assets		5,804	4,647
Equity			
Shareholders' equity		5,059	3,840
Minority interests		745	807
		5,804	4,647

Amounts in accordance with US GAAP

	2006 £m	2005 £m	2004 £m	2003 £m	2002 £m
Total assets	54,623	57,218	55,841	56,400	57,671
Net assets	34,914	34,599	34,429	34,861	35,729
Long-term borrowings	(4,806)	(5,293)	(4,374)	(3,640)	(3,085)
Shareholders' equity	34,653	34,282	34,042	34,116	34,922

Number of employees

	2006	2005	2004	2003	2002
USA	24,726	23,822	23,782	24,036	23,527
Europe	45,758	43,999	44,679	44,559	46,028
International:					
Asia Pacific	17,570	15,991	16,109	18,373	17,289
Japan	3,195	3,098	2,965	2,842	2,952
Middle East, Africa	3,204	5,682	5,134	3,400	5,973
Latin America	5,856	5,664	5,603	5,916	6,876
Canada	2,386	2,472	1,747	1,793	1,854
International	32,211	32,907	31,558	32,324	34,944
	102,695	100,728	100,019	100,919	104,499
Manufacturing	33,235	31,615	31,143	32,459	35,503
Selling	44,484	44,393	44,646	43,978	43,994
Administration	9,024	9,225	9,193	9,550	10,378
Research and development	15,952	15,495	15,037	14,932	14,624
	102,695	100,728	100,019	100,919	104,499

The number of employees is the number of permanent employed staff at the end of the financial period. It excludes those employees who are employed and managed by GlaxoSmithKline on a contract basis.

Exchange rates

As a guide to holders of ADRs, the following tables set out, for the periods indicated, information on the exchange rate of US dollars for Sterling as reported by the Federal Reserve Bank of New York ('noon buying rate').

	2006	2005	2004	2003	2002
Average	1.85	1.81	1.84	1.63	1.51

The average rate for the year is calculated as the average of the noon buying rates on the last day of each month during the year.

	Feb 2007	Jan 2007	Dec 2006	Nov 2006	Oct 2006	Sept 2006
High	1.97	1.98	1.98	1.97	1.91	1.91
Low	1.94	1.93	1.95	1.89	1.85	1.86

The noon buying rate on 23rd February 2007 was £1 = US\$1.96.

Shareholder information

Share price

	2006 £	2005 £	2004 £
At 1st January	14.69	12.22	12.80
High during the year	15.77	15.44	12.99
Low during the year	13.26	11.75	10.42
At 31st December	13.44	14.69	12.22
(Decrease)/Increase	(9)%	20%	(5)%

The table above sets out the middle market closing prices derived from the London Stock Exchange Daily Official List. The company's share price decreased by 9% in 2006 from a price of £14.69 at 1st January 2006 to £13.44 at 31st December 2006. This compares with an increase in the FTSE 100 index of 11% during the year. The share price on 23rd February 2007 was £14.50.

Market capitalisation

The market capitalisation, based on shares in public issue, of GlaxoSmithKline at 31st December 2006 was £77 billion. At that date GSK was the fourth largest company by market capitalisation on the FTSE index.

SmithKline Beecham plc Floating Rate Unsecured Loan Stock 1990/2010

The loan stock is not listed on any exchange but holders may require SmithKline Beecham plc to redeem their loan stock at par, i.e. £1 for every £1 of loan stock held, on the first business day of March, June, September and December. Holders wishing to redeem all or part of their loan stock should complete the notice on the back of their loan stock certificate and return it to the registrar, to arrive at least 30 days before the relevant redemption date.

Taxation

General information concerning the UK and US tax effects of share ownership is set out in 'Taxation information for shareholders' on page 186.

Dividends

GlaxoSmithKline pays dividends quarterly. Details of the dividends declared, the amount and the payment dates are given in Note 14.

Dividends per share

The table below sets out the dividends per share in the last five years.

Year	pence
2006	48.0
2005	44.0
2004	42.0
2003	41.0
2002	40.0

Dividends per ADS

The table below sets out the dividends per ADS in US dollars in the last five years, translated into US dollars at applicable exchange rates.

Year	US\$
2006	1.80
2005	1.57
2004	1.53
2003	1.39
2002	1.24

Dividend calendar

Fourth quarter 2006

Ex-dividend date	14th February 2007
Record date	16th February 2007
Payable	12th April 2007

First quarter 2007

Ex-dividend date	2nd May 2007
Record date	4th May 2007
Payable	12th July 2007

Second quarter 2007

Ex-dividend date	1st August 2007
Record date	3rd August 2007
Payable	11th October 2007

Third quarter 2007

Ex-dividend date	31st October 2007
Record date	2nd November 2007
Payable	10th January 2008

Internet

Information about the company including details of the share price is available on GSK's website at www.gsk.com.

Information made available on the website does not constitute part of this Annual Report.

Investor relations

Investor Relations may be contacted as follows:

UK

980 Great West Road, Brentford, Middlesex TW8 9GS
Tel: +44 (0)20 8047 5000

USA

One Franklin Plaza, PO Box 7929, Philadelphia PA 19101
Tel: 1 888 825 5249 toll free
Tel: +1 215 751 4000 outside the USA

Analysis of shareholdings

Analysis of shareholdings at 31st December 2006

	Number of accounts	% of total accounts	% of total shares	Number of shares
Holding of shares				
Up to 1,000	130,906	71	1	46,807,426
1,001 to 5,000	41,712	23	2	89,668,014
5,001 to 100,000	10,210	5	2	148,081,033
100,001 to 1,000,000	1,048	1	6	366,110,174
Over 1,000,000	490	–	89	5,340,935,201
Totals	184,366	100	100	5,991,601,848
Held by				
Nominee companies	30,702	17	78	4,643,364,576
Investment and trust companies	57	–	1	58,018,488
Insurance companies	14	–	–	162,380
Individuals and other corporate bodies	153,591	83	5	324,318,199
BNY (Nominees) Limited	1	–	12	730,255,527
Held as Treasury shares by GlaxoSmithKline	1	–	4	235,482,678
Totals	184,366	100	100	5,991,601,848

The Bank of New York's holding held through BNY (Nominees) Limited represents the company's ADR programme, whereby each ADS represents two Ordinary Shares of 25p nominal value.

At 23rd February 2007, the number of holders of record of shares in the USA was 1,143 with holdings of 1,508,043 shares, and the number of registered holders of the ADRs was 39,173 with holdings of 423,258,574 ADRs. Certain of these shares and ADRs were held by brokers or other nominees. As a result the number of holders of record or registered holders in the USA is not representative of the number of beneficial holders or of the residence of beneficial holders.

Control of company

As far as is known to the company, it is not directly or indirectly owned or controlled by one or more corporations or by any government. The company does not know of any arrangements, the operation of which might result in a change in control of the company.

Major shareholders have the same voting rights per share as all other shareholders.

Substantial shareholdings

At 23rd February 2007, the company had received notification of the following interests of 3% or more in the shares in issue, excluding Treasury shares:

- BNY (Nominees) Limited holds 846,517,149 shares representing 14.71%. These shares are held on behalf of holders of ADRs, which evidence ADSs
- Legal & General Investment Management Limited holds 218,457,607 shares representing 3.80%
- Barclays PLC holds 240,119,101 shares representing 4.17%.

As far as is known to the company, no other person was the owner of 3% or more of the shares in issue, excluding Treasury Shares of the company.

Directors and Officers

The interests of the Directors and Officers of the company in share options, as defined in the Companies Act 1985, of the company are given in the Remuneration Report (pages 65 to 82).

Exchange controls and other limitations affecting security holders

There are currently no UK laws, decrees or regulations restricting the import or export of capital or affecting the remittance of dividends or other payments to holders of the company's shares who are non-residents of the UK. There are no limitations relating only to non-residents of the UK under English law or the company's Memorandum and Articles of Association on the right to be a holder of, and to vote in respect of, the company's shares.

Documents on display

The Memorandum and Articles of Association of the company and other documents referred to in this Annual Report are available for inspection at the Registered Office of the company.

Publications

In late March 2007 GSK will publish on the website its Corporate Responsibility Report covering performance in areas including community investment, ethics and integrity, access to medicines, R&D and environment health and safety.

Shareholder information

continued

Nature of trading market

The Ordinary Shares of the company were listed on the London Stock Exchange on 27th December 2000. The shares were also listed on the New York Stock Exchange (NYSE) (in the form of American Depositary Shares 'ADSs') from the same date.

The following tables set out, for the periods indicated, the high and low middle market closing quotations in pence for the shares on the London Stock Exchange, and the high and low last reported sales prices in US dollars for the ADSs on the NYSE.

GlaxoSmithKline

	Pence per share	
	High	Low
Quarter ended 31st March 2007*	1493	1344
February 2007*	1493	1386
January 2007	1418	1344
December 2006	1360	1326
November 2006	1427	1331
October 2006	1511	1400
September 2006	1499	1418
Quarter ended 31st December 2006	1511	1326
Quarter ended 30th September 2006	1540	1418
Quarter ended 30th June 2006	1557	1455
Quarter ended 31st March 2006	1577	1424
Quarter ended 31st December 2005	1544	1395
Quarter ended 30th September 2005	1442	1308
Quarter ended 30th June 2005	1377	1201
Quarter ended 31st March 2005	1318	1175
Year ended 31st December 2004	1299	1042
Year ended 31st December 2003	1390	1000
Year ended 31st December 2002	1780	1057

	US dollars per ADS	
	High	Low
Quarter ended 31st March 2007*	58.37	52.66
February 2007*	58.37	54.71
January 2007	55.95	52.66
December 2006	53.73	51.93
November 2006	54.21	51.41
October 2006	56.20	53.21
September 2006	56.76	53.23
Quarter ended 31st December 2006	56.20	51.41
Quarter ended 30th September 2006	57.01	53.23
Quarter ended 30th June 2006	58.38	51.48
Quarter ended 31st March 2006	54.94	50.15
Quarter ended 31st December 2005	53.53	49.16
Quarter ended 30th September 2005	51.28	46.47
Quarter ended 30th June 2005	51.40	45.19
Quarter ended 31st March 2005	50.50	44.48
Year ended 31st December 2004	47.50	39.04
Year ended 31st December 2003	47.40	32.75
Year ended 31st December 2002	50.87	32.86

* to 23rd February 2007

Annual General Meeting 2007

The Queen Elizabeth II Conference Centre, 23rd May 2007
Broad Sanctuary, Westminster,
London SW1P 3EE

The Annual General Meeting is the company's principal forum for communication with private shareholders. In addition to the formal business there will be a presentation by the Chief Executive Officer on the performance of the Group and its future development. There will be opportunity for questions to the Board, and the Chairmen of the Board's committees will take questions on matters relating to those committees.

Investors holding shares in the company through a nominee service should arrange with that nominee service to be appointed as a corporate representative or proxy in respect of their shareholding in order to attend and vote at the meeting.

ADR holders wishing to attend the meeting must obtain a proxy from The Bank of New York which will enable them to attend and vote on the business to be transacted. ADR holders may instruct The Bank of New York as to the way in which the shares represented by their ADRs should be voted by completing and returning the voting card provided by the bank in accordance with the instructions given.

Financial reporting

Financial reporting calendar 2007

Announcement of 1st Quarter Results	April 2007
Announcement of 2nd Quarter Results	July 2007
Announcement of 3rd Quarter Results	October 2007
Preliminary Announcement of Annual Results	February 2008
Publication of Annual Report/Review	March 2008

Results Announcements

Results Announcements are issued to the London Stock Exchange and are available on its news service. Shortly afterwards, they are issued to the media, are made available on the website and sent to the US Securities and Exchange Commission and the NYSE.

Financial reports

The company publishes an Annual Report and, for the investor not needing the full detail of the Report, an Annual Review. These are available from the date of publication on the website.

The Annual Review is sent to all shareholders. Shareholders may also elect to receive the Annual Report by writing to the company's registrars. Alternatively shareholders may elect to receive notification by email of the publication of financial reports by registering on www.shareview.co.uk.

Copies of previous financial reports are available on the website. Printed copies can be obtained from the registrar in the UK and from the GSK Response Center in the USA.

Queries relating to receipt of duplicate copies of GSK's publications should be addressed to the registrars.

Ordinary shares

The company's shares are listed on the London Stock Exchange.

Registrar

The company's registrars are:

Lloyds TSB Registrars
The Causeway, Worthing, West Sussex BN99 6DA
www.shareview.co.uk
Tel: 0870 600 3991 inside the UK
Tel: +44 (0)121 415 7067 outside the UK

The registrars also provide the following services:

- GlaxoSmithKline Investment Plan
- GlaxoSmithKline Individual Savings Account
- GlaxoSmithKline Corporate Sponsored Nominee
- Shareview service
- Shareview dealing service
- Dividend reinvestment plan

Share dealing service

Shareholders may buy or sell shares by internet or telephone through Shareview dealing, a share dealing service provided by Lloyds TSB Registrars. For internet purchases and sales log on to www.shareview.co.uk/dealing and for telephone purchases and sales call 0870 850 0852 (inside the UK only) between 8.00am and 4.30pm, Monday to Friday.

Glaxo Wellcome and SmithKline Beecham corporate PEPs

The Share Centre Limited
Oxford House, Oxford Road, Aylesbury, Bucks HP21 8SZ
Tel: +44 (0)1296 414141

The provision of the details above is not intended to be an invitation or inducement to engage in an investment activity. Advice on share dealing should be obtained from a stockbroker or independent financial adviser.

American Depositary Shares

The company's shares are listed on the NYSE in the form of American Depositary Shares and these are evidenced by American Depositary Receipts (ADRs), each one of which represents two Ordinary Shares.

In general, the NYSE's rules permit the company to follow UK corporate governance practices instead of those that apply in the USA, provided that the company explains any significant variations. This explanation is provided on the company's website.

ADR programme administrator

The ADR programme is administered by:

The Bank of New York
Shareholder Relations
PO Box 11258, Church Street Station
New York NY 10286-1258
www.adrbny.com
Tel: 1 877 353 1154 toll free
Tel: +1 212 815 3700 outside the USA

The administrators also provide Global BuyDIRECT, a direct ADS purchase/sale and dividend reinvestment plan for ADR holders.

GSK Response Center

Tel: 1 888 825 5249 toll free

Taxation information for shareholders

Information for shareholders

A summary of the main tax consequences for holders of shares and ADRs who are citizens or residents of the UK or the USA is set out below. It is not a complete analysis of all the possible tax consequences of purchase or ownership of these securities. It is intended only as a general guide. Holders are advised to consult their advisers with respect to the tax consequences of the purchase and ownership of their shares or ADRs, and the consequences under state and local tax laws in the USA and the implications of the current UK/US Income Tax convention.

This statement is based upon UK and US tax laws and practices at the date of this report.

US holders of ADRs generally will be treated as the owners of the underlying shares for the purposes of the current US/UK double taxation conventions relating to income and gains (Income Tax Convention), estate and gift taxes (Estate and Gift Tax Convention) and for the purposes of the US Internal Revenue Code of 1986, as amended (the Code).

UK shareholders

Taxation of dividends

From 6th April 1999, the rate of tax credits was reduced to one ninth. As a result of compensating reductions in the rate of tax on dividend income, there is no increase in the tax borne by UK resident individual shareholders. Tax credits are, however, no longer repayable to shareholders with a tax liability of less than the associated tax credit.

Taxation of capital gains

UK shareholders may be liable for UK tax on gains on the disposal of shares or ADRs. They may also be entitled to indexation relief and taper relief on such sales. Indexation relief is calculated on the market value of shares at 31st March 1982 and on the cost of any subsequent purchases from the date of such purchase. Indexation relief for individual shareholders ceased on 5th April 1998. Taper relief is available to individual shareholders who hold or are deemed to hold shares for at least three years before they are sold.

Inheritance tax

Individual shareholders may be liable to inheritance tax on the transfer of shares or ADRs. Tax may be charged on the amount by which the value of the shareholder's estate is reduced as a result of any transfer by way of gift or other disposal at less than full market value.

Such a gift or other disposal is subject to both UK inheritance tax and US estate or gift tax. The Estate and Gift Tax Convention would generally provide for tax paid in the USA to be credited against tax payable in the UK.

Stamp duty

UK stamp duty or stamp duty reserve tax (SDRT) will, subject to certain exemptions, be payable on the purchase of shares at a rate of 0.5% of the purchase price. There is a minimum charge of £5 where a stamp duty liability arises.

US shareholders

The following is a summary of certain UK taxation and USA federal income tax considerations that may be relevant to a US holder of shares or ADRs. This summary only applies to a shareholder that holds shares or ADRs as capital assets, is a citizen or resident of the USA or a domestic corporation or that is otherwise subject to United States federal income taxation on a net income basis in respect of the shares or ADRs, and is not resident in the UK for UK tax purposes and does not hold shares for the purposes of a trade, profession or vocation that is carried on in the UK through a branch or agency.

Taxation of dividends

The gross amount of dividends received (without reduction for any UK withholding tax) is treated as foreign source dividend income for US tax purposes. It is not eligible for the dividend received deduction allowed to US corporations. Dividends on ADRs are payable in US dollars; dividends on shares are payable in Sterling. Dividends paid in pounds Sterling will be included in income in the US dollar amount calculated by reference to the exchange rate on the day the dividends are received by the holder. Subject to certain exceptions for short-term or hedged positions, an individual eligible US holder will be subject to US taxation at a maximum rate of 15% in respect of qualified dividends received before 2011. Shareholders are advised to consult their own Tax Advisers to confirm their eligibility.

Taxation of capital gains

Generally, US holders will not be subject to UK capital gains tax, but will be subject to US tax on capital gains realised on the sale or other disposal of shares or ADRs.

Estate and gift taxes

Under the Estate and Gift Tax Convention, a US shareholder is not generally subject to UK inheritance tax.

Stamp duty

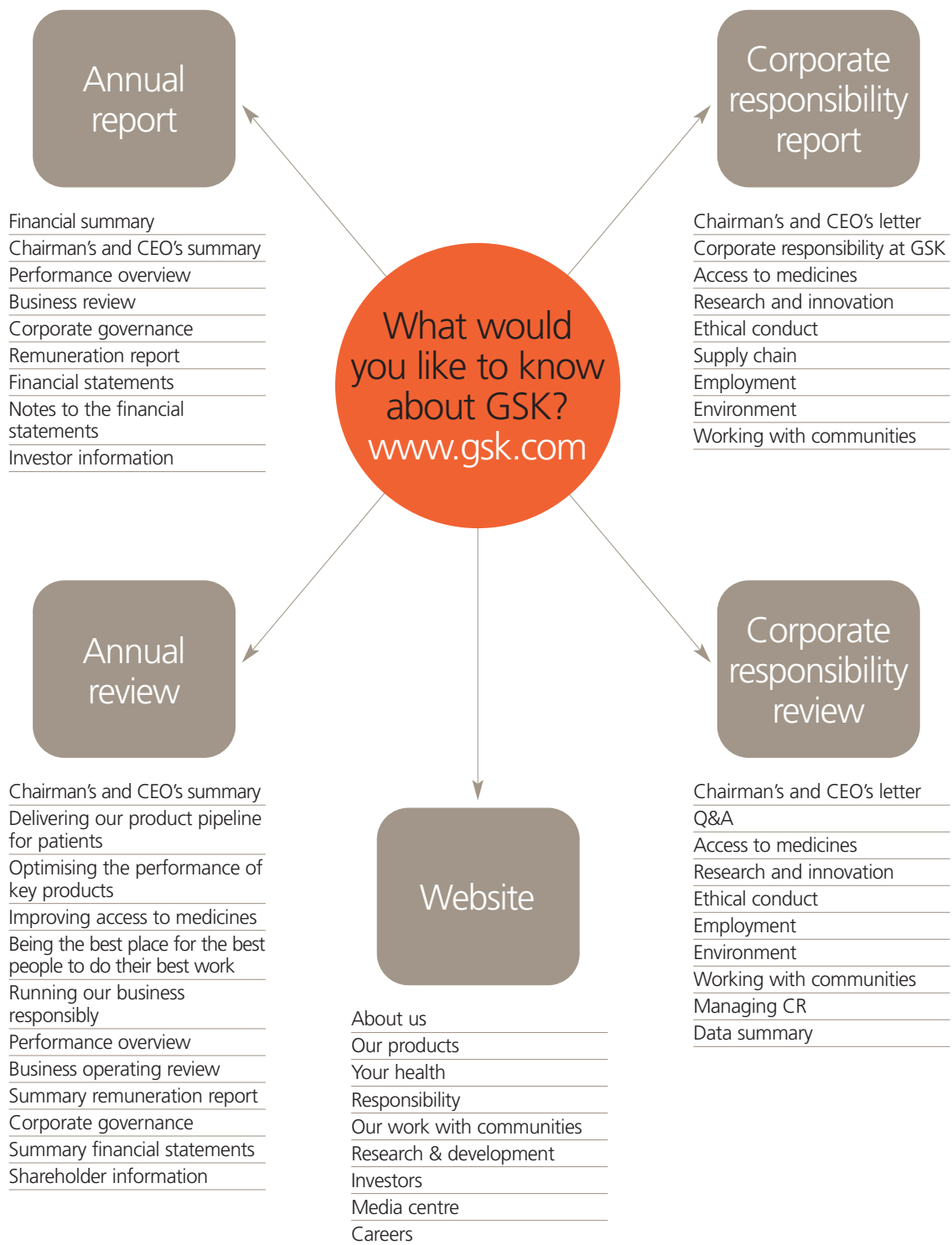
UK stamp duty or SDRT will, subject to certain exemptions, be payable on any issue or transfer of shares to the ADR custodian or depository at a rate of 1.5% of their price (if issued), the amount of any consideration provided (if transferred on sale), or their value (if transferred for no consideration).

No SDRT would be payable on the transfer of an ADR. No UK stamp duty should be payable on the transfer of an ADR provided that the instrument of transfer is executed and remains at all times outside the UK. Any stamp duty on the transfer of an ADR would be payable at a rate of 0.5% of the consideration for the transfer. Any sale of the underlying shares would result in liability to UK stamp duty or, as the case may be, SDRT at a rate of 0.5%. There is a minimum charge of £5 where a stamp duty liability arises.

Terms used in the Annual Report	US equivalent or brief description
Accelerated capital allowances	Tax allowance in excess of depreciation arising from the purchase of fixed assets that delay the charging and payment of tax. The US equivalent of tax depreciation.
Advance Corporation Tax (ACT)	An advance payment of UK tax that was made when dividends are paid. No direct US equivalent.
American Depositary Receipt (ADR)	Receipt evidencing title to an ADS. Each GlaxoSmithKline ADR represents two Ordinary Shares.
American Depositary Shares (ADSs)	Ordinary Shares registered on the New York Stock Exchange.
Basic earnings per share	Basic income per share.
Called-up share capital	Ordinary Shares, issued and fully paid.
CER growth	Growth at constant exchange rates.
Combined Code	Guidelines required by the Listing Rules of the Financial Services Authority to address the principal aspects of Corporate Governance.
The company	GlaxoSmithKline plc.
Creditors	Accounts payable.
Currency swap	An exchange of two currencies, coupled with a subsequent re-exchange of those currencies, at agreed exchange rates and dates.
Debtors	Accounts receivable.
Defined benefit plan	Pension plan with specific employee benefits, often called 'final salary scheme'.
Defined contribution plan	Pension plan with specific contributions and a level of pension dependent upon the growth of the pension fund.
Derivative financial instrument	A financial instrument that derives its value from the price or rate of some underlying item.
Diluted earnings per share	Diluted income per share.
Employee Share Ownership Plan Trusts	Trusts established by the Group to satisfy share-based employee incentive plans.
Finance lease	Capital lease.
Freehold	Ownership with absolute rights in perpetuity.
Gearing ratio	Net debt as a percentage of total equity.
The Group	GlaxoSmithKline plc and its subsidiary undertakings.
Hedging	The reduction of risk, normally in relation to foreign currency or interest rate movements, by making off-setting commitments.
Intangible fixed assets	Assets without physical substance, such as brands, licences, patents, know-how and marketing rights purchased from outside parties.
Non-equity minority interest	Preference shares issued by a subsidiary to outside parties.
Preference shares	Shares issued at varying dividend rates that are treated as outside interests.
Profit	Income.
Profit attributable to shareholders	Net income.
Share capital	Ordinary Shares, capital stock or common stock issued and fully paid.
Shareholders' funds	Shareholders' equity.
Share option	Stock option.
Share premium account	Additional paid-up capital or paid-in surplus (not distributable).
Shares in issue	Shares outstanding.
Statement of recognised income and expense	Statement of comprehensive income.
Stocks	Inventories.
Subsidiary undertaking	An affiliate in which GlaxoSmithKline holds a majority shareholding and/or exercises control.
Treasury share	Treasury stock.
Turnover	Revenue.

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GlaxoSmithKline

Do more, feel better, live longer

Head Office and Registered Office

GlaxoSmithKline plc
980 Great West Road
Brentford, Middlesex TW8 9GS
United Kingdom
Tel: +44 (0)20 8047 5000
www.gsk.com

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