MID AMERICA APARTMENT COMMUNITIES INC
Form 10-Q
August 05, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2010

or

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number: 1-12762

MID-AMERICA APARTMENT COMMUNITIES, INC.
(Exact name of registrant as specified in its charter)

| TENNESSEE | 62-1543819 |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| 6584 POPLAR AVENUE<br>MEMPHIS, TENNESSEE | 38138 |
| (Address of principal executive offices) | (Zip Code) |

(901) 682-6600
(Registrant's telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
þYes ¨ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
þ Yes ¨ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act

| | |
|---|---|
| Large accelerated filer þ | Accelerated filer ¨ |
| Non-accelerated filer ¨ (Do not check if a smaller reporting company) | Smaller Reporting Company ¨ |

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ¨ Yes þ No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

| Class | Number of Shares Outstanding at July 21, 2010 |
|---|---|
| Common Stock, $0.01 par value | 32,798,079 |

MID-AMERICA APARTMENT COMMUNITIES, INC.

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MID-AMERICA APARTMENT COMMUNITIES, INC.
Condensed Consolidated Balance Sheets
June 30, 2010 (Unaudited) and December 31, 2009
(Dollars in thousands, except per share data)

| | June 30, 2010 | December 31, 2009 |
|---|---|---|
| Assets: | | |
| Real estate assets: | | |
| Land | $ 258,394 | $ 255,425 |
| Buildings and improvements | 2,410,202 | 2,364,918 |
| Furniture, fixtures and equipment | 78,577 | 73,975 |
| Capital improvements in progress | 4,256 | 10,517 |
| | 2,751,429 | 2,704,835 |
| Less accumulated depreciation | (836,933) | (788,260) |
| | 1,914,496 | 1,916,575 |
| Land held for future development | 1,306 | 1,306 |
| Commercial properties, net | 8,157 | 8,721 |
| Investments in real estate joint ventures | 12,385 | 8,619 |
| Real estate assets, net | 1,936,344 | 1,935,221 |
| Cash and cash equivalents | 25,245 | 13,819 |
| Restricted cash | 730 | 561 |
| Deferred financing costs, net | 13,658 | 13,369 |
| Other assets | 17,961 | 19,731 |
| Goodwill | 4,106 | 4,106 |
| Assets held for sale | - | 19 |
| Total assets | $ 1,998,044 | $ 1,986,826 |
| Liabilities and Shareholders' Equity: | | |
| Liabilities: | | |
| Notes payable | $ 1,363,195 | $ 1,399,596 |
| Accounts payable | 1,483 | 1,702 |
| Fair market value of interest rate swaps | 56,862 | 51,160 |
| Accrued expenses and other liabilities | 67,608 | 69,528 |
| Security deposits | 8,092 | 8,789 |
| Liabilities associated with assets held for sale | - | 23 |
| Total liabilities | 1,497,240 | 1,530,798 |
| Redeemable stock | 2,900 | 2,802 |
| Shareholders' equity: | | |
| Preferred stock, $0.01 par value per share, 20,000,000 shares authorized, $25 per share liquidation preference; 8.30% Series H Cumulative Redeemable Preferred Stock, 6,200,000 shares authorized, 3,099,999 and 6,200,000 shares issued and outstanding at June 30, 2010 and December 31, 2009, respectively | 31 | 62 |
| Common stock, $0.01 par value per share, 50,000,000 shares authorized; 32,299,493 and 29,095,251 shares issued and outstanding at June 30, 2010 and December 31, 2009, respectively (1) | 322 | 290 |
| Additional paid-in capital | 1,074,147 | 988,642 |
| Accumulated distributions in excess of net income | (541,725) | (510,993) |
| Accumulated other comprehensive income | (56,836) | (47,435) |
| Total Mid-America Apartment Communities, Inc. shareholders' equity | 475,939 | 430,566 |
| Noncontrolling interest | 21,965 | 22,660 |

| | | |
|---|---|---|
| Total Equity | 497,904 | 453,226 |
| Total liabilities and equity | $ 1,998,044 | $ 1,986,826 |

(1) Number of shares issued and outstanding represent total shares of common stock regardless of classification on the consolidated balance sheet.The number of shares classified as redeemable stock on the consolidated balance sheet for June 30, 2010 and December 31, 2009 are 56,336 and 58,038, respectively.

See accompanying notes to consolidated financial statements.

MID-AMERICA APARTMENT COMMUNITIES, INC.
Condensed Consolidated Statements of Operations
Three and six months ended June 30, 2010 and 2009
(Dollars in thousands, except per share data)

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| Operating revenues: | | | | |
| Rental revenues | $ 91,049 | $ 89,593 | $ 181,357 | $ 178,791 |
| Other property revenues | 7,697 | 4,906 | 14,717 | 9,308 |
| Total property revenues | 98,746 | 94,499 | 196,074 | 188,099 |
| Management fee income | 155 | 63 | 291 | 127 |
| Total operating revenues | 98,901 | 94,562 | 196,365 | 188,226 |
| Property operating expenses: | | | | |
| Personnel | 12,717 | 11,962 | 25,075 | 23,326 |
| Building repairs and maintenance | 3,661 | 3,287 | 6,988 | 6,099 |
| Real estate taxes and insurance | 11,321 | 11,059 | 23,219 | 23,043 |
| Utilities | 5,671 | 5,231 | 11,270 | 10,739 |
| Landscaping | 2,518 | 2,490 | 5,033 | 4,794 |
| Other operating | 6,764 | 4,893 | 12,618 | 9,216 |
| Depreciation | 24,943 | 23,818 | 50,023 | 47,403 |
| Total property operating expenses | 67,595 | 62,740 | 134,226 | 124,620 |
| Acquisition expenses | 486 | 107 | 462 | 109 |
| Property management expenses | 4,479 | 4,503 | 8,756 | 8,744 |
| General and administrative expenses | 3,110 | 2,686 | 5,921 | 5,143 |
| Income from continuing operations before non-operating items | 23,231 | 24,526 | 47,000 | 49,610 |
| Interest and other non-property income | 86 | 68 | 401 | 148 |
| Interest expense | (13,993) | (14,472) | (27,884) | (28,701) |
| Loss on debt extinguishment | - | (141) | - | (138) |
| Amortization of deferred financing costs | (648) | (588) | (1,243) | (1,194) |
| Asset impairment | (1,590) | - | (1,590) | - |
| Net casualty gain (loss) and other settlement proceeds | 102 | - | 629 | (144) |
| Income from continuing operations before loss from real estate joint ventures | 7,188 | 9,393 | 17,313 | 19,581 |
| Loss from real estate joint ventures | (298) | (156) | (574) | (352) |
| Income from continuing operations | 6,890 | 9,237 | 16,739 | 19,229 |
| Discontinued operations: | | | | |
| Income from discontinued operations before (loss) gain on sale | - | 326 | - | 747 |
| (Loss) gain on sale of discontinued operations | (2) | 1,155 | (2) | 2,587 |
| Consolidated net income | 6,888 | 10,718 | 16,737 | 22,563 |
| Net income attributable to noncontrolling interests | 228 | 570 | 665 | 1,276 |
| Net income attributable to Mid-America Apartment Communities, Inc. | 6,660 | 10,148 | 16,072 | 21,287 |
| Preferred dividend distributions | 2,704 | 3,217 | 5,920 | 6,433 |
| Premiums and original issuance costs associated with the redemption of preferred stock | 2,573 | - | 2,573 | - |

| | | | | |
|---|---|---|---|---|
| Net income available for common shareholders | $ 1,383 | $ 6,931 | $ 7,579 | $ 14,854 |
| | | | | |
| Weighted average shares outstanding (in thousands): | | | | |
| Basic | 30,628 | 28,105 | 29,883 | 28,095 |
| Effect of dilutive securities | 108 | 79 | 84 | 80 |
| Diluted | 30,736 | 28,184 | 29,967 | 28,175 |
| | | | | |
| Net income available for common shareholders | $ 1,383 | $ 6,931 | $ 7,579 | $ 14,854 |
| Discontinued property operations | 2 | (1,481) | 2 | (3,334) |
| Income from continuing operations available for common shareholders | $ 1,385 | $ 5,450 | $ 7,581 | $ 11,520 |
| | | | | |
| Earnings per share - basic: | | | | |
| Income from continuing operations available for common shareholders | $ 0.04 | $ 0.20 | $ 0.25 | $ 0.41 |
| Discontinued property operations | - | 0.05 | - | 0.12 |
| Net income available for common shareholders | $ 0.04 | $ 0.25 | $ 0.25 | $ 0.53 |
| | | | | |
| Earnings per share - diluted: | | | | |
| Income from continuing operations available for common shareholders | $ 0.04 | $ 0.20 | $ 0.25 | $ 0.41 |
| Discontinued property operations | - | 0.05 | - | 0.12 |
| Net income available for common shareholders | $ 0.04 | $ 0.25 | $ 0.25 | $ 0.53 |
| | | | | |
| Dividends declared per common share | $ 0.615 | $ 0.615 | $ 1.230 | $ 1.230 |

See accompanying notes to consolidated financial statements.

Mid-America Apartment Communities, Inc.
Condensed Consolidated Statements of Cash Flows
Six Months Ended June 30, 2010 and 2009
(Dollars in thousands)

| | 2010 | 2009 |
|---|---|---|
| Cash flows from operating activities: | | |
| Consolidated net income | $ 16,737 | $ 22,563 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| | | |
| Depreciation and amortization of deferred financing costs | 51,266 | 48,597 |
| Stock compensation expense | 1,131 | 623 |
| Redeemable stock issued | 213 | 167 |
| Amortization of debt premium | (180) | (180) |
| Loss from investments in real estate joint ventures | 574 | 352 |
| Loss on debt extinguishment | - | 138 |
| Derivative interest expense | 300 | 616 |
| Loss (gain) on sale of discontinued operations | 2 | (2,587) |
| Asset impairment | 1,590 | - |
| Net casualty (gains) loss and other settlement proceeds | (629) | 144 |
| Changes in assets and liabilities: | | |
| Restricted cash | (169) | (212) |
| Other assets | 1,447 | 3,522 |
| Accounts payable | (234) | 703 |
| Accrued expenses and other | (4,436) | (693) |
| Security deposits | (696) | 181 |
| Net cash provided by operating activities | 66,916 | 73,934 |
| Cash flows from investing activities: | | |
| Purchases of real estate and other assets | (69,718) | (17,729) |
| Improvements to existing real estate assets | (22,595) | (21,707) |
| Renovations to existing real estate assets | (2,858) | (4,249) |
| Development | - | (3,910) |
| Distributions from real estate joint ventures | 1,481 | 95 |
| Contributions to real estate joint ventures | (6,006) | (195) |
| Proceeds from disposition of real estate assets | 48,074 | 14,745 |
| Net cash used in investing activities | (51,622) | (32,950) |
| Cash flows from financing activities: | | |
| Net change in credit lines | (55,000) | 44,831 |
| Proceeds from notes payable | 19,500 | - |
| Principal payments on notes payable | (721) | (44,059) |
| Payment of deferred financing costs | (5,731) | (941) |
| Repurchase of common stock | (813) | (669) |
| Proceeds from issuances of common shares and units | 161,999 | 596 |
| Distributions to noncontrolling interests | (2,927) | (3,112) |
| Dividends paid on common shares | (36,198) | (34,543) |
| Dividends paid on preferred shares | (6,467) | (6,433) |
| Redemption of preferred stock | (77,510) | - |
| Net cash used in financing activities | (3,868) | (44,330) |

| | | | | |
|---|---|---|---|---|
| Net increase (decrease) in cash and cash equivalents | | 11,426 | | (3,346) |
| Cash and cash equivalents, beginning of period | | 13,819 | | 9,426 |
| Cash and cash equivalents, end of period | $ | 25,245 | $ | 6,080 |
| | | | | |
| Supplemental disclosure of cash flow information: | | | | |
| Interest paid | $ | 28,458 | $ | 27,132 |
| Supplemental disclosure of noncash investing and financing activities: | | | | |
| Conversion of units to common shares | $ | 1,190 | $ | - |
| Accrued construction in progress | $ | 2,139 | $ | 4,528 |
| Interest capitalized | $ | - | $ | 109 |
| Marked-to-market adjustment on derivative instruments | $ | (10,063) | $ | 23,361 |
| Reclass of redeemable stock to liabilities | $ | 269 | $ | - |

See accompanying notes to consolidated financial statements.

Mid-America Apartment Communities, Inc.
Notes to Condensed Consolidated Financial Statements
June 30, 2010 (Unaudited) and 2009 (Unaudited)

1. Consolidation and Basis of Presentation

Mid-America Apartment Communities, Inc., or Mid-America, is a self-administered real estate investment trust, or REIT, that owns, acquires, renovates, develops and manages apartment communities in the Sunbelt region of the United States. As of June 30, 2010, we owned or owned interests in a total of 150 multifamily apartment communities comprising 44,462 apartments located in 13 states, including two communities comprising 626 apartments owned through our joint venture, Mid-America Multifamily Fund I, LLC, and two communities comprising 773 apartments owned through our joint venture, Mid-America Multifamily Fund II, LLC.

The accompanying unaudited condensed consolidated financial statements have been prepared by our management in accordance with U.S. generally accepted accounting principles for interim financial information and applicable rules and regulations of the Securities and Exchange Commission, or the SEC, and our accounting policies in effect as of December 31, 2009 as set forth in our annual consolidated financial statements, as of such date. The accompanying unaudited condensed consolidated financial statements include the accounts of Mid-America Apartment Communities, Inc. and its subsidiaries, including Mid-America Apartments, L.P. In our opinion, all adjustments necessary for a fair presentation of the condensed consolidated financial statements have been included and all such adjustments were of a normal recurring nature. All significant intercompany accounts and transactions have been eliminated in consolidation. The results of operations for the three and six month periods ended June 30, 2010 are not necessarily indicative of the results to be expected for the full year. These financial statements should be read in conjunction with our audited financial statements and notes thereto included in our Annual Report on Form 10-K filed with the SEC on February 25, 2010.

The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent liabilities at the dates of the financial statements and the amounts of revenues and expenses during the reporting periods. Actual amounts realized or paid could differ from those estimates.

2. Segment Information

As of June 30, 2010, we owned or had an ownership interest in 150 multifamily apartment communities in 13 different states from which we derived all significant sources of earnings and operating cash flows. Senior management evaluates performance and determines resource allocations by reviewing apartment communities individually and in the following reportable operating segments:

- Large same store communities are generally communities in markets with a population of at least 1 million that we have owned and have been stabilized for at least a full 12 months and have not been classified as held for sale.

- Secondary same store communities are generally communities in markets with populations of less than 1 million that we have owned and have been stabilized for at least a full 12 months and have not been classified as held for sale.

- Non same store communities include recent acquisitions, communities in development or lease-up and communities that have been classified as held for sale.

On the first day of each calendar year we determine the composition of our operating segments for that year which allows us to evaluate full period-over-period operating comparisons. We utilize net operating income, or NOI, in

evaluating the performance. Total NOI represents total property revenues less total property operating expenses, excluding depreciation, for all properties held during the period regardless of their status as held for sale. We believe NOI is a helpful tool in evaluating the operating performance of our segments because it measures the core operations of property performance by excluding corporate level expenses and other items not related to property operating performance.

Revenues, NOI, and assets for each reportable segment for the three and six month periods ended June 30, 2010 and 2009, were as follows (dollars in thousands):

| | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| Revenues | | | | |
| Large Same Store | $ 44,914 | $ 45,214 | $ 89,332 | $ 90,410 |
| Secondary Same Store | 43,617 | 42,694 | 86,567 | 85,009 |
| Non-Same Store | 10,215 | 6,591 | 20,175 | 12,680 |
| Total property revenues | 98,746 | 94,499 | 196,074 | 188,099 |
| Management fee income | 155 | 63 | 291 | 127 |
| Total operating revenues | $ 98,901 | $ 94,562 | $ 196,365 | $ 188,226 |
| | | | | |
| NOI | | | | |
| Large Same Store | $ 25,455 | $ 26,632 | $ 50,433 | $ 53,273 |
| Secondary Same Store | 24,911 | 25,129 | 49,949 | 50,292 |
| Non-Same Store | 5,728 | 4,159 | 11,489 | 8,106 |
| Total NOI | 56,094 | 55,920 | 111,871 | 111,671 |
| Discontinued operations NOI included above | - | (343) | - | (789) |
| Management fee income | 155 | 63 | 291 | 127 |
| Depreciation | (24,943) | (23,818) | (50,023) | (47,403) |
| Acquisition expense | (486) | (107) | (462) | (109) |
| Property management expense | (4,479) | (4,503) | (8,756) | (8,744) |
| General and administrative expense | (3,110) | (2,686) | (5,921) | (5,143) |
| Interest and other non-property income | 86 | 68 | 401 | 148 |
| Interest expense | (13,993) | (14,472) | (27,884) | (28,701) |
| Gain (loss) on debt extinguishment | - | (141) | - | (138) |
| Amortization of deferred financing costs | (648) | (588) | (1,243) | (1,194) |
| Asset impairment | (1,590) | - | (1,590) | - |
| Net casualty gains (loss) and other settlement proceeds | 102 | - | 629 | (144) |
| Loss from real estate joint ventures | (298) | (156) | (574) | (352) |
| Discontinued operations | (2) | 1,481 | (2) | 3,334 |
| Nest income attributable to noncontrolling interests | (228) | (570) | (665) | (1,276) |
| Net income attributable to | | | | |
| Mid-America Apartment Communities, Inc. | $ 6,660 | $ 10,148 | $ 16,072 | $ 21,287 |

| | June 30, 2010 | December 31, 2009 |
|---|---|---|
| Assets | | |
| Large Same Store | $ 920,984 | $ 934,182 |
| Secondary Same Store | 661,380 | 672,692 |
| Non-Same Store | 358,397 | 336,683 |
| Corporate assets | 57,283 | 43,269 |
| Total assets | $ 1,998,044 | $ 1,986,826 |

3. Comprehensive Income and Equity

Total comprehensive income, equity and their components for the six month periods ended June 30, 2010, and 2009, were as follows (dollars in thousands, except per share and per unit data):

| | | | Mid-America Apartment Communities, Inc. Shareholders | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Total | Comprehensive Income | Preferred Stock | Common Stock | Additional Paid-In Capital | Accumulated Distributions in Excess of Net Income | Accumulated Other Comprehensive Income (Loss) | Noncontrolling Interest |
| EQUITY AT DECEMBER 31, 2009 | $ 453,226 | | $ 62 | $ 290 | $ 988,642 | $ (510,993) | $ (47,435) | $ 22,660 |
| Equity Activity Excluding Comprehensive Income: | | | | | | | | |
| Issuance and registration of common shares | 161,963 | | | 32 | 161,931 | | | |
| Shares repurchased and retired | (813) | | | | (813) | | | |
| Exercise of stock options | 33 | | | | 33 | | | |
| Shares issued in exchange for units | - | | | | 1,190 | | | (1,190) |
| Redeemable stock fair market value | (154) | | | | | (154) | | |
| Adjustment for Noncontrolling Interest Ownership in operating partnership | - | | | | (3,053) | | | 3,053 |
| Amortization of unearned compensation | 1,123 | | | | 1,123 | | | |
| Dividends on common stock ($0.615 per share) | (38,157) | | | | | (38,157) | | |
| Dividends on noncontrolling interest units ($0.615 per unit) | (2,861) | | | | | | | (2,861) |
| Redemption of preferred stock | (77,510) | | (31) | | (74,906) | (2,573) | | |
| Dividends on preferred stock | (5,920) | | | | | (5,920) | | |
| Comprehensive income: | | | | | | | | |
| Net income | 16,737 | $ 16,737 | | | | 16,072 | | 665 |
| Other comprehensive income - derivative instruments (cash flow hedges) | (9,763) | (9,763) | | | | | (9,401) | (362) |
| Comprehensive income | 6,974 | $ 6,974 | | | | | | |
| EQUITY BALANCE JUNE 30, 2010 | $ 497,904 | | $ 31 | $ 322 | $ 1,074,147 | $ (541,725) | $ (56,836) | $ 21,965 |

| | | | Mid-America Apartment Communities, Inc. Shareholders | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Total | Comprehensive Income | Preferred Stock | Common Stock | Additional Paid-In Capital | Accumulated Distributions in Excess of Net Income | Accumulated Other Comprehensive Income (Loss) | Noncontrolling Interest |
| EQUITY AT DECEMBER 31, 2008 | $ 442,617 | | $ 62 | $ 282 | $ 954,127 | $ (464,617) | $ (72,885) | $ 25,648 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Equity Activity Excluding Comprehensive Income: | | | | | | | |
| Issuance and registration of common shares | 553 | | | 553 | | | |
| Shares repurchased and retired | (669) | | | (669) | | | |
| Exercise of stock options | 45 | | | 45 | | | |
| Shares issued in exchange for units | - | | | - | - | - | - |
| Redeemable stock fair market value | (3) | | | | (3) | | |
| Adjustment for Noncontrolling Interest Ownership in operating partnership | - | | | 571 | | | (571) |
| Amortization of unearned compensation | 640 | | | 640 | | | |
| Dividends on common stock ($0.615 per share) | (34,546) | | | | (34,546) | | - |
| Dividends on noncontrolling interest units ($0.615 per unit) | (3,112) | | | | | | (3,112) |
| Dividends on preferred stock | (6,433) | | | | (6,433) | | |
| Comprehensive income: | | | | | | | |
| Net income | 22,563 | $ 22,563 | | | 21,287 | | 1,276 |
| Other comprehensive income - derivative instruments (cash flow hedges) | 23,977 | 23,977 | | | | 22,667 | 1,310 |
| Comprehensive income | 46,540 | $ 46,540 | | | | | |
| EQUITY BALANCE JUNE 30, 2009 | $ 445,632 | | $ 62 | $ 282 | $ 955,267 | $ (484,312) | $ (50,218) | $ 24,551 |

The marked-to-market adjustment on derivative instruments is based upon the change of interest rates available for derivative instruments with similar terms and remaining maturities existing at each balance sheet date.

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4. Real Estate Acquisitions

On April 30, 2010, we purchased the Grand Cypress apartments, a 312-unit community located in the Houston, Texas metropolitan statistical area, or MSA.

On August 27, 2008, we purchased 215 units of the 234-unit Village Oaks apartments located in the Tampa, Florida MSA. The remaining 19 units had previously been sold as condominiums and we intend to acquire these units if they become available, and operate them as apartment rentals with the rest of the community. During the remainder of 2008 and during 2009, we acquired 11 of the remaining 19 units. On both February 18, 2010 and June 4, 2010, we acquired one additional unit.

On June 24, 2010, we purchased the 535 Brookwood apartments, a 256-unit community located in the Greenville, South Carolina MSA.

On June 29, 2010, we purchased the Avondale at Kennesaw Farms apartments, a 288-unit community located in the Nashville, Tennessee MSA.

5. Discontinued Operations

As part of our portfolio strategy to selectively dispose of mature assets that no longer meet our investment criteria and long-term strategic objectives, in July 2008, we entered into marketing contracts to list the 440-unit River Trace apartments in Memphis, Tennessee, the 96-unit Riverhills apartments in Grenada, Mississippi, and the 304-unit Woodstream apartments in Greensboro, North Carolina. All of these apartments were subsequently sold during 2009. In accordance with accounting standards governing the disposal of long lived assets, all of these communities are considered discontinued operations in the accompanying condensed consolidated financial statements.

The following is a summary of discontinued operations for the three and six month periods ended June 30, 2010 and 2009, (dollars in thousands):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| Revenues | | | | |
| Rental revenues | $ - | $ 783 | $ - | $ 1,752 |
| Other revenues | - | 16 | - | 53 |
| Total revenues | - | 799 | - | 1,805 |
| Expenses | | | | |
| Property operating expenses | - | 456 | - | 1,016 |
| Depreciation | - | - | - | - |
| Interest expense | - | 17 | - | 42 |
| Total expense | - | 473 | - | 1,058 |
| Income from discontinued operations before gain on sale | - | 326 | - | 747 |
| Gain on sale of discontinued operations | - | 1,155 | - | 2,587 |
| Income from discontinued operations | $ - | $ 1,481 | $ - | $ 3,334 |

6. Share and Unit Information

On June 30, 2010, 32,299,493 common shares and 2,198,090 operating partnership units were outstanding, representing a total of 34,497,583 shares and units. Additionally, we had outstanding options for the purchase of 21,577 shares of common stock at June 30, 2010, of which 10,274 were anti-dilutive. At June 30, 2009, 28,224,270 common shares and 2,403,515 operating partnership units were outstanding, representing a total of 30,627,785 shares and units. Additionally, Mid-America had outstanding options for the purchase of 23,507 shares of common stock at June 30, 2009, of which 16,713 were anti-dilutive.

During the three months ended June 30, 2010, we issued 2,503,600 shares of common stock through our at-the-market, or ATM, program for net proceeds of $131.6 million.

On June 2, 2010, we redeemed 3,100,001 shares of the 6,200,000 issued and outstanding shares of our 8.30% Series H Cumulative Redeemable Preferred Stock, or Series H. The Series H shares being redeemed were redeemed for a $25 per share redemption price plus any accrued and unpaid dividends through and including June 2, 2010. The redemption was funded by proceeds raised through our ATM program.

On July 6, 2010, we announced our plans to redeem the remaining 3,099,999 shares of the issued and outstanding Series H. The shares will be redeemed on August 5, 2010 for a $25 per share redemption price plus any accrued and unpaid dividends through and including August 5, 2010. The redemption will be funded by proceeds through our ATM program.

7. Notes Payable

On June 30, 2010, we had total indebtedness of $1.36 billion, compared to $1.40 billion as of December 31, 2009. Our indebtedness as of June 30, 2010 consisted of both conventional and tax exempt debt. Borrowings were made through individual property mortgages as well as company-wide secured credit facilities.

As of June 30, 2010, approximately 92% of our outstanding debt was borrowed through secured credit facility relationships with Prudential Mortgage Capital, which are credit enhanced by the Federal National Mortgage Association, or FNMA, Financial Federal, which are credit enhanced by the Federal Home Loan Mortgage Corporation, or Freddie Mac, and a $50 million bank facility with a syndicate of banks.

We utilize interest rate swaps and interest rate caps to help manage our current and future interest rate risk and entered into 32 interest rate swaps and 20 interest rate caps as of June 30, 2010, representing notional amounts of $793 thousand and $262 thousand, respectively.

The following table summarizes our debt structure as of June 30, 2010 (dollars in thousands):

| | Borrowed Balance | Effective Rate | Contract Maturity |
|---|---|---|---|
| Fixed Rate Debt | | | |
| Individual property mortgages | $ 88,845 | 5.8% | 5/14/2020 |
| Tax-exempt | 11,070 | 5.3% | 12/1/2028 |
| FNMA conventional credit facilities | 50,000 | 4.7% | 3/31/2017 |
| Credit facility balances managed with interest rate swaps | | | |
| LIBOR-based interest rate swaps | 767,000 | 5.3% | 1/2/2013 |
| BMA-based interest rate swaps | 26,165 | 4.5% | 2/17/2012 |
| Total fixed rate debt | 943,080 | 5.3% | 2/1/2014 |
| | | | |
| Variable Rate Debt | | | |
| FNMA conventional credit facilities | 259,318 | 0.9% | 9/23/2014 |
| FNMA tax-free credit facilities | 64,350 | 1.1% | 3/1/2014 |
| Feddie Mac credit facilities | 81,247 | 0.8% | 6/28/2013 |
| Freddie Mac mortgage | 15,200 | 3.7% | 12/10/2015 |
| Total variable rate debt | 420,115 | 1.0% | 6/12/2014 |
| | | | |
| Total Outstanding Debt | $ 1,363,195 | 4.0% | 3/13/2014 |

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8. Derivatives and Hedging Activities

Risk Management Objective of Using Derivatives

We are exposed to certain risk arising from both our business operations and economic conditions. We principally manage our exposures to a wide variety of business and operational risks through management of our core business activities. We manage economic risks, including interest rate, liquidity, and credit risk primarily by managing the amount, sources, and duration of our debt funding and the use of derivative financial instruments. Specifically, we enter into derivative financial instruments to manage exposures that arise from business activities that result in the payment of future contractual and forecasted cash amounts, principally related to our borrowings, the value of which are determined by changing interest rates.

Cash Flow Hedges of Interest Rate Risk

Our objectives in using interest rate derivatives are to add stability to interest expense and to manage our exposure to interest rate movements. To accomplish this objective, we use interest rate swaps and interest rate caps as part of our interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable amounts from a counterparty in exchange for us making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount. Interest rate caps designated as cash flow hedges involve the receipt of variable amounts from a counterparty if interest rates rise above the strike rate on the contract in exchange for an up front premium.

The effective portion of changes in the fair value of derivatives designated and that qualify as cash flow hedges is recorded in accumulated other comprehensive income and is subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. During the three and six months ended June 30, 2010 and 2009, such derivatives were used to hedge the variable cash flows associated with existing variable-rate debt. The ineffective portion of the change in fair value of the derivatives is recognized directly in earnings. During the three months ended June 30, 2010 and 2009, we recorded ineffectiveness of $155,000 and $1.1 million, respectively, and during the six months ended June 30, 2010 and 2009, $259,000 and $676,000, respectively, as an increase to interest expense attributable to a mismatch in the underlying indices of the derivatives and the hedged interest payments made on our variable-rate debt.

We also have nine interest rate caps, totaling a notional amount of $56.3 million, where only the changes in intrinsic value are recorded in accumulated other comprehensive income. Changes in fair value of these interest rate caps due to changes in time value (e.g. volatility, passage of time, etc.) are excluded from effectiveness testing and are recognized directly in earnings. During the three months ended June 30, 2010 and 2009, we recorded a gain of less than $1,000 and $101,000, respectively, and during the six months ended June 30, 2010 and 2009, a loss of $31,000 and a gain of $109,000, respectively, due to changes in the time value of these interest rate caps.

Amounts reported in accumulated other comprehensive income related to derivatives designated in qualifying cash flow hedges will be reclassified to interest expense as interest payments are made on our variable-rate debt. During the next twelve months, we estimate that an additional $28.1 million will be reclassified to earnings as an increase to interest expense, which primarily represents the difference between our fixed interest rate swap payments and the projected variable interest rate swap payments.

As of June 30, 2010 we had the following outstanding interest rate derivatives that were designated as cash flow hedges of interest rate risk:

| | Interest Rate | Number of Instruments | Notional |
|---|---|---|---|

| Derivatives | | |
|---|---|---|
| Interest Rate Cap | 20 | $ 262,286,000 |
| Interest Rate Swap | 32 | $ 793,165,000 |

Non-designated Hedges

We do not use derivatives for trading or speculative purposes and currently do not have any derivatives that are not designated as qualifying accounting hedges under ASC 815.

Tabular Disclosure of Fair Values of Derivative Instruments on the Balance Sheet

The table below presents the fair value of our derivative financial instruments as well as their classification on the Condensed Consolidated Balance Sheet as of June 30, 2010 and December 31, 2009, respectively:

Fair Values of Derivative Instruments on the Condensed Consolidated Balance Sheet as of June 30, 2010 and December 31, 2009 (dollars in thousands)

| | Asset Derivatives | | | Liability Derivatives | | |
|---|---|---|---|---|---|---|
| | | June 30, 2010 | December 31, 2009 | | June 30, 2010 | December 31, 2009 |
| Derivatives designated as hedging instruments | Balance Sheet Location | Fair Value | Fair Value | Balance Sheet Location | Fair Value | Fair Value |
| Interest rate contracts | Other assets | $ 3,269 | $ 3,430 | Fair market value of interest rate swaps | $ 56,862 | $ 51,160 |
| Total derivatives designated as hedging instruments | | $ 3,269 | $ 3,430 | | $ 56,862 | $ 51,160 |

Tabular Disclosure of the Effect of Derivative Instruments on the Income Statement

The tables below present the effect of our derivative financial instruments on the Condensed Consolidated Statements of Operations for the three and six months ended June, 2010 and 2009, respectively.

Effect of Derivative Instruments on the Condensed Consolidated Statements of Operations for the Three and Six Months Ended June 30, 2010 and 2009 (dollars in thousands)

| Derivatives in Cash Flow Hedging Relationships | Amount of Gain or (Loss) Recognized in OCI on Derivatives (Effective Portion) | | Location of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion) | Amount of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion) | | Location of Gain or (Loss) Recognized in Income on Derivatives (Ineffective Portion and Amount Excluded from Effectiveness Testing) | Amount of Gain (Loss) Recognize Income on Derivat (Ineffective Porti and Amount Excluded Effectiveness Test | |
|---|---|---|---|---|---|---|---|---|
| | 2010 | 2009 | | 2010 | 2009 | | 2010 | 2009 |
| Three months ended June 30, | | | | | | | | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Interest rate contracts | $ (14,955) | $ 10,924 | Interest expense | $ (8,624) | $ (7,597) | Interest expense | $ (154) | $ (1,01 |
| Total derivatives in cash flow hedging relationships | $ (14,955) | $ 10,924 | | $ (8,624) | $ (7,597) | | $ (154) | $ (1,01 |
| Six months ended June 30, | | | | | | | | |
| Interest rate contracts | $ (27,788) | $ 10,052 | Interest expense | $ (18,026) | $ (13,924) | Interest expense | $ (290) | $ (56 |
| Total derivatives in cash flow hedging relationships | $ (27,788) | $ 10,052 | | $ (18,026) | $ (13,924) | | $ (290) | $ (56 |

Credit-risk-related Contingent Features

As of June 30, 2010, derivatives that were in a net liability position and subject to credit-risk-related contingent features had a termination value of $61.6 million, which includes accrued interest but excludes any adjustment for nonperformance risk. These derivatives had a fair value, gross of asset positions, of $56.9 million at June 30, 2010.

Certain of our derivative contracts contain a provision where if we default on any of our indebtedness, including default where repayment of the indebtedness has not been accelerated by the lender, then we could also be declared in default on our derivative obligations. As of June 30, 2010, we had not breached the provisions of these agreements. If we had breached these provisions, we could have been required to settle our obligations under the agreements at their termination value of $21.4 million.

Certain of our derivative contracts are credit enhanced by either Federal National Mortgage Association, or FNMA, and the Federal Home Loan Mortgage Corporation, or Freddie Mac. These derivative contracts require that our credit enhancing party maintain credit ratings above a certain level. If our credit support providers were downgraded below Baa1 by Moody's or BBB+ by Standard & Poor's, or S&P, we may be required to either post 100% collateral or settle the obligations at their termination value of $61.6 million as of June 30, 2010. Both FNMA and Freddie Mac are currently rated Aaa by Moody's and AAA by S&P, and therefore, the provisions of this agreement have not been breached and no collateral has been posted related to these agreements as of June 30, 2010.

Although our derivative contracts are subject to master netting arrangements, which serve as credit mitigants to both us and our counterparties under certain situations, we do not net our derivative fair values or any existing rights or obligations to cash collateral on the consolidated balance sheet.

See also discussions in Item 1. Financial Statements – Notes to Consolidated Financial Statements, Note 9.

9. Fair Value Disclosure of Financial Instruments

Cash and cash equivalents, restricted cash, accounts payable, accrued expenses and other liabilities and security deposits are carried at amounts that reasonably approximate their fair value due to their short term nature.

Fixed rate notes payable at June 30, 2010 and December 31, 2009, totaled $150 million and $81 million, respectively, and had estimated fair values of $127 million and $74 million (excluding prepayment penalties), respectively, based upon interest rates available for the issuance of debt with similar terms and remaining maturities as of June 30, 2010 and December 31, 2009. The carrying value of variable rate notes payable (excluding the effect of interest rate swap and cap agreements) at June 30, 2010 and December 31, 2009, totaled $1,213 million and $1,318 million, respectively, and had estimated fair values of $1,118 million and $1,193 million (excluding prepayment penalties), respectively, based upon interest rates available for the issuance of debt with similar terms and remaining maturities as of June 30, 2010 and December 31, 2009.

On January 1, 2008, we adopted FASB ASC 820 Fair Value Measurements and Disclosures, or ASC 820. ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. ASC 820 applies to reported balances that are required or permitted to be measured at fair value under existing accounting pronouncements; accordingly, the standard does not require any new fair value measurements of reported balances.

ASC 820 emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, ASC 820

establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that we have the ability to access. Level 2 inputs are inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the asset or liability (other than quoted prices), such as interest rates, foreign exchange rates, and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, which are typically based on an entity's own assumptions, as there is little, if any, related market activity. In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

Derivative financial instruments

Currently, we use interest rate swaps and interest rate caps (options) to manage our interest rate risk. The valuation of these instruments is determined using widely accepted valuation techniques including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, including interest rate curves and implied volatilities. The fair values of interest rate swaps are determined using the market standard methodology of netting the discounted future fixed cash receipts (or payments) and the discounted expected variable cash payments (or receipts). The variable cash payments (or receipts) are based on an expectation of future interest rates (forward curves) derived from observable market interest rate curves.

The fair values of interest rate options are determined using the market standard methodology of discounting the future expected cash receipts that would occur if variable interest rates rise above the strike rate of the caps. The variable interest rates used in the calculation of projected receipts on the cap are based on an expectation of future interest rates derived from observable market interest rate curves and volatilities.

To comply with the provisions of ASC 820, we incorporate credit valuation adjustments to appropriately reflect both our own nonperformance risk and the respective counterparty's nonperformance risk in the fair value measurements. In adjusting the fair value of our derivative contracts for the effect of nonperformance risk, we have considered the impact of netting and any applicable credit enhancements, such as collateral postings, thresholds, mutual puts and guarantees.

Although we have determined that the majority of the inputs used to value our derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with our derivatives utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by ourself and our counterparties. In prior periods, we classified our derivative valuations within the Level 3 fair value hierarchy because those valuations contain certain Level 3 inputs (e.g. credit spreads). Commencing with the six months ended June 30, 2010, we determined that the significance of the impact of the credit valuation adjustments made to our derivative contracts, which determination was based on the fair value of each individual contract, was not significant to the overall valuation. As a result, all of our derivatives held as of June 30, 2010 were transferred from Level 3 of the fair value hierarchy to Level 2 at the beginning of the six months ended June 30, 2010.

The table below presents a reconciliation of the beginning and ending balances of assets and liabilities having fair value measurements based on significant other observable inputs (Level 2) and significant unobservable inputs (Level 3) for the six months ended June 30, 2010.

Reconciliation of Level 2 and Level 3 Fair Value Measurements for the Six Months Ended June 30, 2010 (dollars in thousands)

| | Assets | | Liabilities | |
|---|---|---|---|---|
| | Level 2 | Level 3 | Level 2 | Level 3 |
| Beginning fair value as of 12/31/2009 | $ - | $ 3,430 | $ - | $ 51,160 |
| Transfers in | 3,430 | - | 51,160 | - |
| Purchase, issuances and settlements | 4,200 | - | - | - |
| Transfers out | - | (3,430) | - | (51,160) |
| Total gains/(loss) | (4,361) | - | (5,702) | - |
| Ending fair value as of 6/30/2010 | $ 3,269 | $ - | $ 56,862 | $ - |

The table below presents our assets and liabilities measured at fair value on a recurring basis as of June 30, 2010 and December 31, 2009, aggregated by the level in the fair value hierarchy within which those measurements fall.

Assets and Liabilities Measured at Fair Value on a Recurring Basis at June 30, 2010 (dollars in thousands)

| | Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Balance at June 30, 2010 |
|---|---|---|---|---|
| Assets | | | | |
| Derivative financial instruments | $ —| $ 3,269 | $ —| $ 3,269 |
| Liabilities | | | | |
| Derivative financial instruments | $ —| $ 56,862 | $ —| $ 56,862 |

Assets and Liabilities Measured at Fair Value on a Recurring Basis at December 31, 2009
(dollars in thousands)

| | Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Balance at December 31, 2009 |
|---|---|---|---|---|
| Assets | | | | |
| Derivative financial instruments | $ —$ | —$ | 3,430 | $ 3,430 |
| Liabilities | | | | |
| Derivative financial instruments | $ —$ | —$ | 51,160 | $ 51,160 |

The fair value estimates presented herein are based on information available to management as of June 30, 2010 and December 31, 2009. These estimates are not necessarily indicative of the amounts we could ultimately realize. See also discussions in Item 1. Financial Statements – Notes to Consolidated Financial Statements, Note 8.

10. Asset Impairment

During the three months ended June 30, 2010, we received an offer to purchase our 276-unit Cedar Mill apartment community. As a result of the offer received and management's reconsideration of its long-term intentions related to this property, MAA determined that an impairment indicator existed. As the estimated undiscounted future cash flows were no longer sufficient to recover the asset carrying amount, we recorded an impairment charge of $1,590,000 during the three months ended June 30, 2010 to adjust the asset carrying value to estimated fair value. The operations of the Cedar Mill community are included in our secondary same store operating segment.

11. Recent Accounting Pronouncements

Impact of Recently Issued Accounting Standards

In June 2009, the FASB issued ASC 105-10, Generally Accepted Accounting Principles – Overall, which establishes the FASB Accounting Standards Codification, or the Codification, as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with U.S. generally accepted accounting principles, or GAAP. Rules and interpretive releases of the SEC under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. All guidance contained in the Codification carries an equal level of authority. The Codification superseded all existing non-SEC accounting and reporting standards. All other non-grandfathered, non-SEC accounting literature not included in the Codification is non-authoritative. The FASB will not issue new standards in the form of Statements, FASB Staff Positions or Emerging Issues Task Force Abstracts. Instead, it will issue Accounting Standards Updates, or ASUs. The FASB will not consider ASUs as authoritative in their own right. ASUs will serve only to update the Codification, provide background information about the guidance and provide the bases for conclusions on the change(s) in the Codification. We adopted ASC 105-10 effective July 1, 2009 and all references made to FASB guidance throughout this document have been updated for the Codification.

In April 2008, the FASB issued ASC 825-10-65-1, Interim Disclosures About Fair Market Value of Financial Instruments, or ASC 825-10-65-1, which extends the disclosure requirements concerning the fair value of financial instruments to interim financial statements of publicly traded companies. ASC 825-10-65-1 is effective for interim financial periods ending after June 15, 2009, and the required disclosures are included in Note 8 to the condensed consolidated financial statements.

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In June 2008, the FASB issued ASC 810-10-05, Amendments to FASB Interpretation No. 46(R), or ASC 810-10-05, which amends events that would require reconsidering whether an entity is a variable interest entity; it amends the criteria used to determine the primary beneficiary of a variable interest entity; and it expands disclosures about an enterprise's involvement in variable interest entities. ASC 810-10-05 is effective for annual reporting periods beginning after November 15, 2009 and earlier application is prohibited. We adopted ASC 810-10-05 effective January 1, 2010. The adoption did not have a material impact on our consolidated financial condition or results of operations taken as a whole.

12. Subsequent Events

8.30% Series H Cumulative Redeemable Preferred Stock, or Series H

On July 6, 2010, we announced the redemption of the 3,099,999 issued and outstanding shares of our Series H for a $25 per share redemption price plus any accrued and unpaid dividends through and including the redemption date. The shares were redeemed on August 5, 2010 and the redemption was funded by proceeds raised through our ATM program.

Real Estate Acquisitions

On April 30, 2010, we purchased the Grand Cypress apartments, a 312-unit community located in the Houston, Texas MSA. On July 13, 2010 we contributed Grand Cypress to Mid-America Multifamily Fund II, LLC, one of our joint ventures.

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

The following discussion should be read in conjunction with the condensed consolidated financial statements and notes appearing elsewhere in this report. Historical results and trends which might appear in the condensed consolidated financial statements should not be interpreted as being indicative of future operations.

Forward Looking Statements

We consider this and other sections of this Quarterly Report on Form 10-Q to contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, with respect to our expectations for future periods. Forward looking statements do not discuss historical fact, but instead include statements related to expectations, projections, intentions or other items related to the future. Such forward-looking statements include, without limitation, statements concerning property acquisitions and dispositions, development and renovation activity as well as other capital expenditures, capital raising activities, rent growth, occupancy, and rental expense growth. Words such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estima and variations of such words and similar expressions are intended to identify such forward-looking statements. Such statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements to be materially different from the results of operations or plans expressed or implied by such forward-looking statements. Such factors include, among other things, unanticipated adverse business developments affecting us, or our properties, adverse changes in the real estate markets and general and local economies and business conditions. Although we believe that the assumptions underlying the forward-looking statements contained herein are reasonable, any of the assumptions could be inaccurate, and therefore such forward-looking statements included in this report may not prove to be accurate. In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that the results or conditions described in such statements or our objectives and plans will be achieved.

The following factors, among others, could cause our future results to differ materially from those expressed in the forward-looking statements:

- inability to generate sufficient cash flows due to market conditions, changes in supply and/or demand, competition, uninsured losses, changes in tax and housing laws, or other factors;
- increasing real estate taxes and insurance costs;
- failure of new acquisitions to achieve anticipated results or be efficiently integrated into us;
- failure of development communities to lease-up as anticipated;
- inability of a joint venture to perform as expected;

- inability to acquire additional or dispose of existing apartment units on favorable economic terms;
- losses from catastrophes in excess of our insurance coverage;
- unexpected capital needs;
- inability to attract and retain qualified personnel;
- potential liability for environmental contamination;
- adverse legislative or regulatory tax changes;
- litigation and compliance costs associated with laws requiring access for disabled persons;
- imposition of federal taxes if we fail to qualify as a REIT under the Internal Revenue Code in any taxable year or foregone opportunities to ensure REIT status;
- inability to acquire funding through the capital markets;
- inability to pay required distributions to maintain REIT status due to required debt payments;
- changes in interest rate levels, including that of variable rate debt, such as extensively used by us;

for the same period in 2015. A decline in sales of Harvoni was partially offset by sales of our TAF-based products, Genvoya, Odefsey and Descovy, and an increase in sales of Truvada.

Product sales in Europe were $1.6 billion for the three months ended June 30, 2016, compared to $2.0 billion for the same period in 2015. The decrease was primarily due to lower Sovaldi and Harvoni sales volume and a higher proportion of sales in countries with lower Sovaldi and Harvoni average net selling prices. In addition, foreign currency exchange rates, net of hedges, had an unfavorable impact of $104 million on our product sales for the three months ended June 30, 2016, compared to the same period in 2015.

Product sales in Japan, which consist of Sovaldi and Harvoni, were $619 million for the three months ended June 30, 2016, compared to $62 million for the same period in 2015. Sovaldi and Harvoni were launched in Japan in May and September 2015, respectively.

Product sales in other international locations were $531 million for the three months ended June 30, 2016, compared to $515 million for the same period in 2015, primarily due to continued launches of our HCV products.

Product sales for the six months ended June 30, 2016

Total product sales were $15.3 billion for the six months ended June 30, 2016, compared to $15.5 billion for the same period in 2015, primarily due to a decrease in antiviral product sales.

Antiviral product sales were $14.3 billion for the six months ended June 30, 2016, compared to $14.6 billion for the same period in 2015. HIV and other antiviral product sales were $6.0 billion for the six months ended June 30, 2016, compared to $5.2 billion for the same period in 2015 primarily due to sales of our TAF-based products, Genvoya, Descovy, and Odefsey. HCV product sales were $8.3 billion for the six months ended June 30, 2016, compared to $9.4 billion for the same period in 2015 primarily due to a decline in sales of Harvoni.

Other product sales, which include sales of Ranexa, Letairis and AmBisome, were $1.0 billion for the six months ended June 30, 2016, compared to $912 million for the same period in 2015.

Foreign currency exchange, net of hedges, had an unfavorable impact on our product sales of $300 million for the six months ended June 30, 2016, compared to the same period in 2015. Of our total product sales, 40% were generated outside of the U.S. during the six months ended June 30, 2016. We faced exposure to movements in foreign currency exchange rates, primarily in the Euro. We use foreign currency exchange contracts to hedge a percentage of our foreign currency exposure.

Product sales in the U.S. were $9.3 billion for the six months ended June 30, 2016, compared to $10.8 billion for the same period in 2015. A decline in sales of Harvoni was partially offset by an increase in sales of Sovaldi, sales of Genvoya, which was launched in the U.S. in November 2015, and an increase in sales of Truvada where we have seen an increase in the use of Truvada as a preventive treatment for HIV.

Product sales in Europe were $3.2 billion for the six months ended June 30, 2016, compared to $3.8 billion for the same period in 2015. The decrease was primarily due to lower HCV products average net selling prices and lower Sovaldi sales volume. In addition, foreign currency exchange rates, net of hedges, had an unfavorable impact of $245 million on our product sales for the six months ended June 30, 2016, compared to the same period in 2015.

Product sales in Japan, which consist of Sovaldi and Harvoni, were $1.7 billion for the six months ended June 30, 2016, compared to $62 million for the same period in 2015. Sovaldi and Harvoni were launched in Japan in May and September 2015, respectively. During the six months ended June 30, 2016, sales volume declined from early launch levels reached during the second half of 2015 and pricing for Sovaldi and Harvoni was adjusted to reflect a mandatory price reduction of 32% that was effective April 1, 2016.

Product sales in other international locations were $1.1 billion for the six months ended June 30, 2016, compared to $879 million for the same period in 2015, primarily due to continued launches of our HCV products.

The following table summarizes the period over period changes in our net product sales by product:

| (In millions, except percentages) | Three Months Ended June 30, 2016 | 2015 | Change | Six Months Ended June 30, 2016 | 2015 | Change |
|---|---|---|---|---|---|---|
| Antiviral products: | | | | | | |
| Harvoni | $2,564 | $3,608 | (29)% | $5,581 | $7,187 | (22)% |
| Sovaldi | 1,358 | 1,291 | 5 % | 2,635 | 2,263 | 16 % |
| Truvada | 942 | 849 | 11 % | 1,840 | 1,620 | 14 % |
| Atripla | 673 | 782 | (14)% | 1,348 | 1,516 | (11)% |
| Stribild | 429 | 447 | (4)% | 906 | 803 | 13 % |
| Complera/Eviplera | 368 | 367 | — % | 749 | 687 | 9 % |
| Genvoya | 302 | — | * | 460 | — | * |
| Viread | 287 | 271 | 6 % | 559 | 505 | 11 % |
| Epclusa | 64 | — | * | 64 | — | * |
| Descovy | 61 | — | * | 61 | — | * |
| Odefsey | 58 | — | * | 69 | — | * |
| Other antiviral | 20 | 16 | 25 % | 37 | 38 | (3)% |
| Total antiviral products | 7,126 | 7,631 | (7)% | 14,309 | 14,619 | (2)% |
| Other products: | | | | | | |
| Letairis | 203 | 176 | 15 % | 378 | 327 | 16 % |
| Ranexa | 153 | 141 | 9 % | 297 | 258 | 15 % |
| AmBisome | 85 | 103 | (17)% | 171 | 188 | (9)% |
| Zydelig | 41 | 30 | 37 % | 90 | 56 | 61 % |
| Other | 43 | 45 | (4)% | 87 | 83 | 5 % |
| Total product sales | $7,651 | $8,126 | (6)% | $15,332 | $15,531 | (1)% |

* Percentage not meaningful

Following is additional discussion related to the key period over period changes in net product sales by product:

- Harvoni

Net product sales of Harvoni for the three and six months ended June 30, 2016 accounted for 36% and 39% of our total antiviral product sales, respectively.

For the three months ended June 30, 2016, net product sales of Harvoni were $1.5 billion in the U.S., $512 million in Europe, $448 million in Japan, and $130 million in other international locations, compared to $2.8 billion in the U.S., $623 million in Europe and $159 million in other international locations for the same period in 2015. In the U.S., the decrease was primarily due to lower average net selling price and lower sales volume compared to Harvoni's early launch levels during the prior year. The number of patients that started treatment with Harvoni in the U.S. peaked in the first half of 2015 indicative of the rapid initiation of treatment for many warehoused patients. Harvoni was launched in the U.S. in October 2014. During the second quarter, we also had a favorable revision to our Harvoni sales return reserve of $181 million. In Europe, the decrease was primarily due to lower sales volume and a higher proportion of sales from countries that have lower average net selling prices. Additionally, we have seen a slight decline in average treatment duration, as countries are treating more patients with lower fibrosis scores who qualify for an eight-week treatment duration. In Japan, we launched Harvoni in September 2015. In other international locations, the decrease was primarily due to higher sales from countries that have lower average net selling prices.

For the six months ended June 30, 2016, net product sales of Harvoni were $2.9 billion in the U.S., $1.1 billion in Europe, $1.3 billion in Japan, and $298 million in other international locations, compared to $5.8 billion in the U.S., $1.1 billion in Europe and $245 million in other international locations for the same period in 2015. In the U.S., the decrease was primarily due to lower sales volume and lower average net selling price. The number of patients that started treatment with Harvoni in the U.S. peaked in the first half of 2015 indicative of the rapid initiation of

treatment

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for many warehoused patients. In Europe, higher sales volume were offset by a higher proportion of sales from countries that have lower average net selling prices and unfavorable foreign exchange currency rates, net of hedges. In Japan, the increase was driven by the launch of Harvoni in September 2015. In other international locations, the increase was driven by the continued launches of Harvoni.

•Sovaldi

Net product sales of Sovaldi for the three and six months ended June 30, 2016 accounted for 19% and 18% of our total antiviral product sales, respectively.

For the three months ended June 30, 2016, net product sales of Sovaldi were $775 million in the U.S., $263 million in Europe, $171 million in Japan, and $149 million in other international locations, compared to $615 million in the U.S., $522 million in Europe, $62 million in Japan and $92 million in other international locations for the same period in 2015. In the U.S., the increase includes a favorable revision to our Sovaldi sales return reserve of $98 million and higher sales volume, partially offset by lower average net selling price. In Europe, the decrease was primarily due to lower sales volume and lower average net selling price. In Japan, the increase is reflective of the launch of Sovaldi in May 2015. In other international locations, the increase was primarily driven by the continued launches of Sovaldi.

For the six months ended June 30, 2016, net product sales of Sovaldi were $1.4 billion in the U.S., $543 million in Europe, $373 million in Japan, and $299 million in other international locations, compared to $1.0 billion in the U.S., $1.0 billion in Europe, $62 million in Japan and $160 million in other international locations for the same period in 2015. In the U.S., the increase was primarily driven by higher sales volume. In Europe, the decrease was primarily due to lower sales volume and lower average net selling price. In Japan, the increase was primarily driven by the launch of Sovaldi in May 2015. In other international locations, the increase was primarily driven by the continued launches of Sovaldi.

•Truvada

Net product sales of Truvada for both the three and six months ended June 30, 2016 accounted for 13% of our antiviral product sales.

For the three months ended June 30, 2016, net product sales of Truvada were $631 million in the U.S., $245 million in Europe and $66 million in other international locations, compared to $500 million in the U.S., $277 million in Europe and $72 million in other international locations for the same period in 2015. The increase was primarily driven by higher average net selling price and higher sales volume primarily driven by increased usage of Truvada for pre-exposure prophylaxis or PrEP.

For the six months ended June 30, 2016, net product sales of Truvada were $1.2 billion in the U.S., $496 million in Europe and $137 million in other international locations, compared to $909 million in the U.S., $578 million in Europe and $133 million in other international locations for the same period in 2015. The increase was primarily driven by higher average net selling price and higher sales volume primarily driven by increased usage of Truvada for PrEP.

•Atripla

Net product sales of Atripla for both the three and six months ended June 30, 2016 accounted for 9% of our total antiviral product sales.

For the three months ended June 30, 2016, net product sales of Atripla were $479 million in the U.S. and $140 million in Europe, compared to $549 million in the U.S. and $178 million in Europe for the same period in 2015. The decrease was primarily due to declines in sales volume as doctors prescribed newer regimens, including tenofovir disoproxil fumarate (TDF) and TAF-based regimens. The efavirenz component of Atripla sales, which has a gross margin of zero, comprised $246 million of our Atripla sales for the three months ended June 30, 2016, compared to $290 million for the same period in 2015.

For the six months ended June 30, 2016, net product sales of Atripla were $968 million in the U.S. and $283 million in Europe, compared to $1.0 billion in the U.S. and $372 million in Europe for the same period in 2015. The decrease was primarily due to declines in sales volume as doctors prescribed newer regimens, including TDF and TAF-based regimens. The efavirenz component of Atripla sales, which has a gross margin of zero, comprised $494 million of our Atripla sales for the six months ended June 30, 2016, compared to $558 million for the same period of 2015.

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- Stribild

Net product sales of Stribild for both the three and six months ended June 30, 2016 accounted for 6% of our total antiviral product sales.

For the three months ended June 30, 2016, net product sales of Stribild were $326 million in the U.S. and $84 million in Europe, compared to $364 million in the U.S. and $65 million in Europe for the same period in 2015. The decrease was primarily due to the launch of our new TAF-based product, Genvoya.

For the six months ended June 30, 2016, net product sales of Stribild were $702 million in the U.S. and $165 million in Europe, compared to $646 million in the U.S. and $126 million in Europe for the same period in 2015. The increase was primarily driven by higher sales volume.

- TAF-based regimens - Genvoya, Descovy, and Odefsey

Net product sales of our recently launched TAF-based regimens for the three and six months ended June 30, 2016 accounted for 6% and 4% of our total antiviral product sales, respectively. Genvoya was launched in the U.S. and Europe in November 2015. Descovy was launched in the U.S. and Europe in April 2016. Odefsey was launched in the U.S. in March 2016 and approved by European Commission in June 2016.

For the three months ended June 30, 2016, net product sales of Genvoya were $302 million, primarily driven by sales in the U.S. of $268 million.

For the six months ended June 30, 2016, net product sales of Genvoya were $460 million, primarily driven by sales in the U.S. of $409 million.

While we have seen continued strength in our HIV and other product sales, there has been a slowing of HCV patient treatments in the U.S. and earlier launch markets in Europe since the first half of 2015 when Harvoni had been recently launched, indicative of the rapid initiation of treatment for many warehoused patients. In addition, we have seen lower average net selling prices for our HCV products primarily as a result of a mix shift towards payer segments in the U.S. that receive significantly higher rebates and discounts and towards countries with lower average net selling prices in Europe. We expect a continued gradual trend toward shorter duration of HCV treatments and could experience a decline in market share due to increased competition in the future. We anticipate that total net product sales for the full year 2016 will be lower than net product sales for 2015.

Cost of Goods Sold and Product Gross Margin

The following table summarizes our cost of goods sold and product gross margin:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| (In millions, except percentages) | 2016 | 2015 | 2016 | 2015 |
| Cost of goods sold | $864 | $998 | $2,057 | $1,880 |
| Product gross margin | 89 % | 88 % | 87 % | 88 % |

The product gross margin change in the three months ended June 30, 2016 compared to the same period in 2015 was primarily due to the reversal of the $200 million litigation reserve recorded in the first quarter of 2016 following a favorable court decision.

Operating Expenses

The following table summarizes the period over period changes in our R&D expenses and SG&A expenses:

| | Three Months Ended June 30, | | | Six Months Ended June 30, | | |
|---|---|---|---|---|---|---|
| (In millions, except percentages) | 2016 | 2015 | Change | 2016 | 2015 | Change |
| Research and development expenses | $1,484 | $818 | 81 % | $2,749 | $1,514 | 82 % |
| Selling, general and administrative expenses | $890 | $812 | 10 % | $1,575 | $1,457 | 8 % |

Research and Development Expenses

R&D expenses summarized above consist primarily of clinical studies performed by contract research organizations, materials and supplies, licenses and fees, up-front and milestone payments under collaboration arrangements,

personnel costs, including salaries, benefits and stock-based compensation and overhead allocations consisting of various support and facilities-related costs.

We do not track total R&D expenses by product candidate, therapeutic area or development phase. However, we manage our R&D expenses by identifying the R&D activities we anticipate will be performed during a given period and then prioritizing efforts based on scientific data, probability of successful development, market potential, available human and capital resources and other considerations. We continually review our R&D pipeline and the status of development and, as necessary, reallocate resources among the R&D portfolio that we believe will best support the future growth of our business.

R&D expenses for the three months ended June 30, 2016 increased by $666 million or 81%, compared to the same period in 2015, primarily due to $624 million related to our purchase of Nimbus and a FDA priority review voucher, and the overall progression of clinical studies.

R&D expenses for the six months ended June 30, 2016 increased by $1.2 billion or 82%, compared to the same period in 2015, primarily due to $1.0 billion related to our collaboration and acquisition related expenses, including our purchase of Nimbus, our license and collaboration agreement with Galapagos NV, the purchase of a FDA priority review voucher, and the overall progression of clinical studies. In addition, during the first quarter of 2016, we recorded a $114 million in-process R&D impairment charge related to momelotinib.

Selling, General and Administrative Expenses

SG&A expenses relate to sales and marketing, finance, human resources, legal and other administrative activities. Expenses are primarily comprised of facilities and overhead costs, outside marketing, advertising and legal expenses, and other general and administrative costs.

SG&A expenses for the three months ended June 30, 2016 increased by $78 million or 10%, compared to the same period in 2015, primarily due to expenses to support new product launches and geographic expansion.

SG&A expenses for the six months ended June 30, 2016 increased by $118 million or 8%, compared to the same period in 2015, primarily due to expenses to support new product launches and geographic expansion. These increases were partially offset by a net decrease of $103 million in Branded Prescription Drug (BPD) fee expenses. The first quarter of 2016 and 2015 were favorably impacted by a credit to the BPD fee of $191 million and $100 million, respectively, based on receipt of the Internal Revenue Service (IRS) invoices. The BPD fee is calculated based on select government sales during each calendar year as a percentage of total industry government sales.

Interest Expense

Interest expense for the three months ended June 30, 2016 was $227 million, compared to $140 million for the same period in 2015. Interest expense for the six months ended June 30, 2016 was $457 million, compared to $293 million for the same period in 2015. The increases in both periods were primarily due to interest expense incurred related to the issuances of senior unsecured notes in September 2015. For more information see Note 9, Debt and Credit Facility of the Notes to Condensed Consolidated Financial Statements in this quarterly report.

Provision for Income Taxes

Provision for income taxes for the three months ended June 30, 2016 was $902 million, compared to $1.0 billion for the same period in 2015. Our effective tax rate was 20.5% for the three months ended June 30, 2016, compared to 18.4% for the same period in 2015.

Provision for income taxes for the six months ended June 30, 2016 was $1.8 billion, compared to $1.9 billion for the same period in 2015. Our effective tax rate was 20.6% for the six months ended June 30, 2016, compared to 17.9% for the same period in 2015.

The effective tax rates for the three and six months ended June 30, 2016 were higher than the effective tax rates for the same periods in 2015 primarily due to changes in the geographic mix of earnings.

The effective tax rates for the three and six months ended June 30, 2016 and 2015 differed from the U.S. federal statutory rate of 35% primarily due to certain operating earnings from non-U.S. subsidiaries that are considered indefinitely reinvested and tax credits, partially offset by state taxes, our portion of the non-tax deductible BPD fee and amortization expense of the intangible asset related to sofosbuvir for which we receive no tax benefit. We do not provide for U.S. income taxes on undistributed earnings of our foreign operations that are intended to be indefinitely reinvested in our foreign subsidiaries.

Liquidity and Capital Resources

We believe that our existing capital resources, supplemented by our cash flows generated from operating activities will be adequate to satisfy our capital needs for the foreseeable future. The following table summarizes our cash, cash equivalents and marketable securities and working capital:

| (In millions) | June 30, 2016 | December 31, 2015 |
|---|---|---|
| Cash, cash equivalents and marketable securities | $24,616 | $ 26,208 |
| Working capital | $7,909 | $ 14,872 |

Cash, Cash Equivalents and Marketable Securities

Cash, cash equivalents and marketable securities totaled $24.6 billion at June 30, 2016, a decrease of $1.6 billion when compared to $26.2 billion at December 31, 2015. A discussion of the key drivers of our cash flows follows below.

Of the total cash, cash equivalents and marketable securities at June 30, 2016, approximately $23.4 billion was generated from operations in foreign jurisdictions and is intended for use in our foreign operations. We do not rely on unrepatriated earnings as a source of funds for our domestic business as we expect to have sufficient cash flow and borrowing capacity in the United States to fund our domestic operational and strategic needs.

Working Capital

Working capital was $7.9 billion at June 30, 2016, compared to $14.9 billion at December 31, 2015. The decrease of $7.0 billion was primarily due to a decline in cash and cash equivalents as described below.

Cash Flows

The following table summarizes our cash flow activities:

| | Six months ended June 30, | |
|---|---|---|
| (In millions) | 2016 | 2015 |
| Cash provided by (used in): | | |
| Operating activities | $8,853 | $11,359 |
| Investing activities | $(5,393) | $(5,851 ) |
| Financing activities | $(9,912) | $(8,063 ) |

Cash Provided by Operating Activities

Cash provided by operating activities was $8.9 billion for the six months ended June 30, 2016. Cash flows from operating activities represent the cash receipts and disbursements related to all of our activities other than investing and financing activities. Operating cash flow is derived by adjusting our net income of $7.1 billion for non-cash items of $739 million and changes in operating assets and liabilities of $1.1 billion. The changes in operating assets and liabilities were primarily due to an increase in accrued government and other rebates resulting from timing of payments. We expect our cash flow from operations to decrease in the future as we continue to make cash payments related to accrued government and other rebates as well as milestone payments.

For the six months ended June 30, 2016, compared to the same period in 2015, the decrease in cash provided by operating activities was primarily due to lower net income and a decrease in the change of accrued liabilities resulting from timing of payments.

Cash Used in Investing Activities

Cash used in investing activities for the six months ended June 30, 2016 was $5.4 billion, consisting of $4.7 billion net purchases of marketable securities, $357 million of other investments related to our agreement with Galapagos and $381 million in capital expenditures related to the expansion of our business.

Cash used in investing activities for the six months ended June 30, 2015 was $5.9 billion, consisting of $5.6 billion in net purchases of marketable securities and $295 million in capital expenditures related to the expansion of our business.

Cash Used in Financing Activities

Cash used in financing activities for the six months ended June 30, 2016 was $9.9 billion, consisting primarily of $9.0 billion utilized to repurchase our common stock under our stock repurchase programs and $1.2 billion used to pay cash dividends. Of our $9.0 billion common stock repurchases, $5.0 billion and $4.0 billion were through an accelerated stock repurchase program and open market transactions, respectively. We anticipate stock repurchases in the second half of 2016 to be lower than the first half of 2016.

In February 2016, our Board of Directors authorized a $12.0 billion share repurchase program (2016 Program) under which repurchases may be made in the open market or in privately negotiated transactions. We started repurchases under our 2016 Program in April 2016.

Cash used in financing activities for the six months ended June 30, 2015 was $8.1 billion, consisting primarily of $3.9 billion used to repurchase our common stock under our stock repurchase programs and $3.9 billion for our warrant settlements.

Debt and Credit Facility

In May 2016, we terminated our existing revolving credit facility and entered into a new $2.5 billion, five-year revolving credit facility maturing in May 2021. The facility can be used for working capital requirements and for general corporate purposes, including, without limitation, acquisitions. As of June 30, 2016, there were no amounts outstanding under the revolving credit facility.

As of June 30, 2016, there were 9 million shares of our common stock underlying our warrants associated with our May 2016 Convertible Senior Notes (the 2016 Warrants). The 2016 Warrants have a strike price of $27.86 per share and expire during the 40 trading-day period commencing on August 1, 2016 and ending on September 26, 2016. On July 27, 2016, we exercised our option to settle the warrants in cash.

The summary of our borrowings under various financing arrangements is included in Item 1, Note 9 Debt and Credit Facility of our Notes to Condensed Consolidated Financial Statements of this Form 10-Q. There were no other material changes to our debt and credit facility during the first six months of 2016.

Critical Accounting Policies, Estimates and Judgments

The preparation of our Condensed Consolidated Financial Statements requires us to make estimates and judgments that affect the reported amounts in the financial statements and related disclosures. On an ongoing basis, management evaluates its significant accounting policies and estimates. We base our estimates on historical experience and on various market-specific and other relevant assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ significantly from these estimates. Estimates are assessed each period and updated to reflect current information. A summary of our critical accounting policies and estimates is presented in Part II, Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2015. There were no material changes to our critical accounting policies and estimates during the six months ended June 30, 2016.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements as defined in Item 303(a)(4)(ii) of Regulation S-K.

Recent Accounting Pronouncements

See Item 1, Note 1 Summary of Significant Accounting Policies of our Notes to Condensed Consolidated Financial Statements.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in our market risk during the six months ended June 30, 2016 compared to the disclosures in Part II, Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2015.

As of June 30, 2016, our accounts receivable in Southern Europe, specifically Greece, Italy, Portugal and Spain, totaled approximately $630 million, of which $171 million were greater than 120 days past due, including $36 million greater than 365 days past due. To date, we have not experienced significant losses with respect to the collection of our accounts receivable. We believe that our allowance for doubtful accounts was adequate at June 30, 2016. However, we will continue to monitor the European economic environment for collectability issues related to our outstanding receivables.

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Item 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

An evaluation as of June 30, 2016 was carried out under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of our "disclosure controls and procedures," which are defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act), as controls and other procedures of a company that are designed to ensure that the information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective at June 30, 2016.

Changes in Internal Control over Financial Reporting

Our management, including our Chief Executive Officer and Chief Financial Officer, has evaluated any changes in our internal control over financial reporting that occurred during the quarter ended June 30, 2016, and has concluded that there was no change during such quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Limitations on the Effectiveness of Controls

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, if any, within a company have been detected. Accordingly, our disclosure controls and procedures are designed to provide reasonable, not absolute, assurance that the objectives of our disclosure control system are met and, as set forth above, our Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as of the end of the period covered by this report, that our disclosure controls and procedures were effective to provide reasonable assurance that the objectives of our disclosure control system were met.

PART II. OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

For a description of our significant pending legal proceedings, please see Item 1, Note 10 Commitments and Contingencies of our Notes to Condensed Consolidated Financial Statements.

Item 1A. RISK FACTORS

In evaluating our business, you should carefully consider the following risks in addition to the other information in this Quarterly Report on Form 10-Q. A manifestation of any of the following risks could materially and adversely affect our business, results of operations and financial condition. We note these factors for investors as permitted by the Private Securities Litigation Reform Act of 1995. It is not possible to predict or identify all such factors and, therefore, you should not consider the following risks to be a complete statement of all the potential risks or uncertainties that we face.

A substantial portion of our revenues is derived from sales of products to treat HCV and HIV. If we are unable to maintain or continue increasing sales of these products, our results of operations may be adversely affected.

During the six months ended June 30, 2016, sales of Harvoni, Sovaldi and Epclusa for the treatment of HCV accounted for approximately 54% of our total product sales. We cannot be certain if prior year sales of our HCV products are indicative of future sales. Sales of our HCV products peaked in the first quarter of 2015 as warehoused patients started treatment in large numbers. Since then, the number of new patient starts has diminished. In the second quarter of 2016, we saw slowing of patient starts in the U.S. commercial segment and some of the earlier launch markets of Europe. We expect the revenue per patient to decline as a result of payers opening coverage to patients with lower fibrosis scores in exchange for additional discounts, a shift in our payer mix toward more deeply discounted government payer segments in the United States and countries with a lower average net selling price in Europe, competition and a decrease in the average duration of treatment as fewer patients are treated for 24 weeks and more patients are treated for 8 weeks. We also could experience a decline in market share due to increased competition.

In addition, future sales of Harvoni, Sovaldi and Epclusa are difficult to estimate because demand depends, in part, on the extent of reimbursement of our HCV products by private and government payers. In light of continued fiscal and debt crises experienced by several countries in the European Union and Japan, governments have announced or implemented measures to manage healthcare expenditures. We may continue to experience global pricing pressure which could result in larger discounts or rebates on our products or delayed reimbursement, which negatively impacts our product sales and results of operations. Also, private and public payers can choose to exclude Harvoni, Sovaldi or Epclusa from their formulary coverage lists or limit the types of patients for whom coverage will be provided, which would negatively impact the demand for, and revenues of, Harvoni, Sovaldi and Epclusa. Any change in the formulary coverage, reimbursement levels or discounts or rebates offered on our HCV products to payers may impact our anticipated revenues. We expect pricing pressure in the HCV market to continue. For example, the government of Japan implemented mandatory price reductions on Harvoni and Sovaldi effective as of April 1, 2016. If we are unable to achieve our forecasted HCV sales, our HCV product revenues and results of operations could be negatively affected, and our stock price could experience significant volatility.

We receive a substantial portion of our revenue from sales of our products for the treatment of HIV infection, particularly our single-tablet regimen products, Genvoya, Odefsey, Stribild, Complera/Eviplera and Atripla. During the six months ended June 30, 2016, sales of our HIV products accounted for approximately 39% of our total product sales. Most of our HIV products contain tenofovir alafenamide (TAF), tenofovir disoproxil fumarate and/or emtricitabine, which belong to the nucleoside class of antiviral therapeutics. In addition, if the treatment paradigm for HIV changes, causing nucleoside-based therapeutics to fall out of favor, or if we are unable to maintain or increase our HIV product sales, our results of operations would likely suffer and we would likely need to scale back our operations, including our spending on research and development (R&D) efforts.

We may be unable to sustain or increase sales of our HCV or HIV products for any number of reasons including, but not limited to, the following:

- As our HCV and HIV products are used over a longer period of time in many patients and in combination with other products, and additional studies are conducted, new issues with respect to safety, resistance and interactions with

other drugs may arise, which could cause us to provide additional warnings or contraindications on our labels, narrow our approved indications or halt sales of a product, each of which could reduce our revenues.

- As our products mature, private insurers and government payers often reduce the amount they will reimburse patients for these products, which increases pressure on us to reduce prices.
- If physicians do not see the benefit of our HCV or HIV products, the sales of our HCV or HIV products will be limited.
- As new or generic products are introduced into major markets, our ability to maintain pricing and market share may be affected. For example, tenofovir disoproxil fumarate, one of the active pharmaceutical ingredients in Stribild,

Complera/Eviplera, Atripla and Truvada, is expected to face generic competition in the United States and European Union in 2017, which may have an impact on our business and results of operations.

If we fail to commercialize new products or expand the indications for existing products, our prospects for future revenues may be adversely affected.

If we do not introduce new products or increase sales of our existing products, we will not be able to increase or maintain our total revenues nor continue to expand our research and development efforts. Drug development is inherently risky and many product candidates fail during the drug development process. For example, in January 2016 we announced that we terminated our Phase 2 study of simtuzumab for the treatment of idiopathic pulmonary fibrosis.

In the first quarter of 2016, we filed our NDA and MAA in the United States and European Union for the approval of TAF for the treatment of chronic hepatitis B virus (HBV) infection. These marketing applications may not be approved by the regulatory authorities on a timely basis, or at all. Even if marketing approval is granted for these products, there may be significant limitations on their use. Further, we may be unable to file our marketing applications for new products.

Our inability to accurately predict demand for our products, uptake of new products or fluctuations in customer inventories makes it difficult for us to accurately forecast sales and may cause our forecasted revenues and earnings to fluctuate, which could adversely affect our financial results and our stock price.

We may be unable to accurately predict demand for our products, including the uptake of new products, as demand is dependent on a number of factors. For example, our HCV products, Harvoni, Sovaldi and Epclusa, represent a significant change in the treatment paradigm for HCV-infected patients due to the shortened duration of treatment and the elimination of pegylated interferon injection and ribavirin in most patient populations. Because these products represent a cure and competitors' HCV products have entered the market, revenues from our HCV products in 2016 and beyond are difficult for us and investors to estimate. Demand for Harvoni, Sovaldi and Epclusa will depend on the availability of HCV patients and the extent of reimbursement of our HCV products by private and public payers in the United States and other countries. In addition, private and public payers can choose to exclude Harvoni, Sovaldi or Epclusa from their formulary coverage lists or limit the types of patients for whom coverage will be provided, which would negatively impact the demand for and revenues of Harvoni, Sovaldi and Epclusa. We have experienced, and we may continue to experience, pricing pressure in the United States, European Union, Japan and other countries. Any change in the formulary coverage, reimbursement levels or discounts or rebates offered on our HCV products to payers may negatively impact our anticipated revenues. In addition, because rebate claims for product discounts are made by payers one or two quarters in arrears, we estimate the rebates we will be required to pay in connection with sales during a particular quarter based on claims data from prior quarters. In the first quarter of 2016, we received higher than expected prior quarter rebate claims. This had the effect of lowering our revenue for the quarter. Because HCV-related revenues are difficult to predict, investors may have widely varying expectations that may be materially higher or lower than our actual revenues. To the extent our HCV product revenues exceed or fall short of these expectations, our stock price may experience significant volatility.

In the six months ended June 30, 2016, approximately 92% of our product sales in the United States were to three wholesalers, AmerisourceBergen Corp., McKesson Corp. and Cardinal Health, Inc. The U.S. wholesalers with whom we have entered into inventory management agreements make estimates to determine end user demand and may not be completely effective in matching their inventory levels to actual end user demand. As a result, changes in inventory levels held by those wholesalers can cause our operating results to fluctuate unexpectedly if our sales to these wholesalers do not match end user demand. In addition, inventory is held at retail pharmacies and other non-wholesaler locations with whom we have no inventory management agreements and no control over buying patterns. Adverse changes in economic conditions or other factors may cause retail pharmacies to reduce their inventories of our products, which would reduce their orders from wholesalers and, consequently, the wholesalers' orders from us, even if end user demand has not changed. For example, during the fourth quarter of 2015, strong wholesaler and sub-wholesaler purchases of our HIV products resulted in inventory draw-down by wholesalers and sub-wholesalers in the first quarter of 2016. As inventory in the distribution channel fluctuates from quarter to quarter, we may continue to see fluctuations in our earnings and a mismatch between prescription demand for our

products and our revenues.

In addition, the non-retail sector in the United States, which includes government institutions, including state AIDS Drug Assistance Programs (ADAPs), Veterans Administration (VA), correctional facilities and large health maintenance organizations, tends to be even less consistent in terms of buying patterns and often causes quarter over quarter fluctuations that do not necessarily mirror patient demand for our products. Federal and state budget pressures, including sequestration, as well as the annual grant cycles for federal and state funds, may cause purchasing patterns to not reflect patient demand of our products. For example, in the first quarters of certain prior years, we observed large non-retail purchases of our HIV products by a number of state ADAPs that exceeded patient demand. We believe such purchases were driven by the grant cycle for federal ADAP funds. Additionally, during the second half of 2015, we experienced fluctuations in VA new HCV patient starts and purchasing patterns due to VA funding. We expect to continue to experience fluctuations in the purchasing patterns of our non-retail customers which may result

in fluctuations in our product sales, revenues and earnings in the future. In light of the global economic downturn and budget crises faced by many European countries, we have observed variations in purchasing patterns induced by cost containment measures in Europe. We believe these measures have caused some government agencies and other purchasers to reduce inventory of our products in the distribution channels, which has decreased our revenues and caused fluctuations in our product sales and earnings. We may continue to see this trend in the future.

Our results of operations may be adversely affected by current and potential future healthcare reforms.

Legislative and regulatory changes to government prescription drug procurement and reimbursement programs occur relatively frequently in the United States and foreign jurisdictions. In the United States, we, along with other pharmaceutical manufacturers of branded drug products, are required to pay a portion of an industry fee (also known as the Branded Prescription Drug (BPD) fee), calculated based on select government sales during the year as a percentage of total industry government sales. The amount of the annual BPD fee imposed on the pharmaceutical industry as a whole is $3.0 billion in 2016, which will increase to $4.0 billion in 2017, increase to a peak of $4.1 billion in 2018, and then decrease to $2.8 billion in 2019 and thereafter. Our BPD fee expenses were $414 million in 2015, $590 million in 2014 and $110 million in 2013. We expect our portion of the BPD fee to increase as the total annual industry-wide fee increases through 2017 and drug patents expire on major drugs of other companies. The BPD fee is not tax deductible. In addition, even though not addressed in the healthcare reform legislation, discussions continue at the federal level on legislation that would either allow or require the federal government to directly negotiate price concessions from pharmaceutical manufacturers or set minimum requirements for Medicare Part D pricing. Further, certain states have proposed legislation that seeks to regulate pharmaceutical drug pricing. If such proposed legislation is passed, we may experience additional pricing pressures on our products.

In addition, state Medicaid programs could request additional supplemental rebates on our products as a result of the increase in the federal base Medicaid rebate. Private insurers could also use the enactment of these increased rebates to exert pricing pressure on our products, and to the extent that private insurers or managed care programs follow Medicaid coverage and payment developments, the adverse effects may be magnified by private insurers adopting lower payment schedules.

Our existing products are subject to reimbursement from government agencies and other third parties. Pharmaceutical pricing and reimbursement pressures may reduce profitability.

Successful commercialization of our products depends, in part, on the availability of governmental and third-party payer reimbursement for the cost of such products and related treatments in the markets where we sell our products. Government health authorities, private health insurers and other organizations generally provide reimbursement. In the United States, the European Union, Japan and other significant or potentially significant markets for our products and product candidates, government authorities and third-party payers are increasingly attempting to limit or regulate the price of medical products and services. A significant portion of our sales of the majority of our products are subject to significant discounts from list price. See also our risk factor "A substantial portion of our revenues is derived from sales of products to treat HCV and HIV. If we are unable to maintain or continue increasing sales of these products, our results of operations may be adversely affected."

Pricing for pharmaceutical products has come under increasing scrutiny by governments, legislative bodies and enforcement agencies. These activities may result in actions that have the effect of reducing prices or harming our business or reputation.

In July 2014, we received a letter from the U.S. Senate Committee on Finance (Senate Committee) requesting information and supporting documentation from us related to Sovaldi and the pricing of Sovaldi in the United States. The letter raised concerns about our approach to pricing Sovaldi, its affordability and its impact on federal government spending and public health. In December 2015, the Senate Committee released the results of the investigation, which alleged that we engaged in a revenue-driven pricing strategy in setting Sovaldi’s price. Gilead disagrees with many of the conclusions in the report. In January 2016, we received a letter from the Massachusetts Attorney General advising that their office is considering whether our pricing of Sovaldi and Harvoni may constitute an unfair trade practice in violation of Massachusetts law. In February 2016, the Massachusetts Attorney General’s office served us with a Civil Investigative Demand (CID) requesting that we produce documents related to our HCV products. In July 2016, the Massachusetts Attorney General’s office notified us of their decision to suspend Gilead’s

obligations under the CID until further notice. In February 2016, we received a subpoena from the U.S. Attorney's Office for the District of Massachusetts requesting documents related to our support of 501(c)(3) organizations that provide financial assistance to patients, and for our HCV products, documents concerning our provision of financial assistance to patients. Other companies have disclosed similar inquiries. We are cooperating with this inquiry. It is possible that the results of the Senate Committee investigation and any actions taken by the U.S. Department of Justice, the Massachusetts Attorney General or other state governments could result in civil penalties or injunctive relief, negative publicity or other negative actions that could harm our reputation, reduce demand for Harvoni, Sovaldi, Epclusa or other sofosbuvir containing products and/or reduce coverage of Harvoni, Sovaldi, Epclusa or other sofosbuvir containing products, including by federal health care programs such as Medicare

and Medicaid and state health care programs. If any or all of these events occur, our business and stock price could be materially and adversely affected.

Approximately 40% of our product sales occur outside the United States, and currency fluctuations and hedging expenses may cause our earnings to fluctuate, which could adversely affect our stock price.

Because a significant percentage of our product sales are denominated in foreign currencies, primarily the Euro and Yen, we face exposure to adverse movements in foreign currency exchange rates. When the U.S. dollar strengthens against these foreign currencies, the relative value of sales made in the respective foreign currency decreases. Conversely, when the U.S. dollar weakens against these currencies, the relative value of such sales increases. Overall, we are a net receiver of foreign currencies and, therefore, benefit from a weaker U.S. dollar and are adversely affected by a stronger U.S. dollar.

We use foreign currency exchange forward and option contracts to hedge a percentage of our forecasted international sales, primarily those denominated in the Euro and Yen. We also hedge certain monetary assets and liabilities denominated in foreign currencies, which reduces but does not eliminate our exposure to currency fluctuations between the date a transaction is recorded and the date that cash is collected or paid. Foreign currency exchange, net of hedges, had an unfavorable impact of $115 million and $300 million on our product sales for the three and six months ended June 30, 2016, respectively, compared to the same periods in 2015.

We cannot predict future fluctuations in the foreign currency exchange rates of the U.S. dollar. If the U.S. dollar appreciates significantly against certain currencies and our hedging program does not sufficiently offset the effects of such appreciation, our results of operations will be adversely affected and our stock price may decline.

Additionally, the expenses that we recognize in relation to our hedging activities can also cause our earnings to fluctuate. The level of hedging expenses that we recognize in a particular period is impacted by the changes in interest rate spreads between the foreign currencies that we hedge and the U.S. dollar.

We face significant competition.

We face significant competition from large global pharmaceutical and biotechnology companies, specialized pharmaceutical firms and generic drug manufacturers.

Our HCV products, Harvoni, Sovaldi and Epclusa, compete with Viekira Pak (ombitasvir, paritaprevir and ritonavir tablets co-packaged with dasabuvir tablets) and Viekira XR (dasabuvir, ombitasvir, paritaprevir and ritonavir) marketed by AbbVie Inc. (AbbVie), Zepatier (elbasvir and grazoprevir) marketed by Merck & Co. Inc. (Merck), Daklinza (daclastavir) marketed by BMS and Olysio (simeprevir) marketed by Janssen Therapeutics.

Our HIV products compete primarily with products from ViiV Healthcare (ViiV), which markets fixed-dose combination products that compete with Descovy, Odefsey, Genvoya, Stribild, Complera/Eviplera, Atripla and Truvada. For example, two products marketed by ViiV, Tivicay (dolutegravir), an integrase inhibitor, and Triumeq, a single-tablet triple-combination antiretroviral regimen, could adversely impact sales of our HIV products. In addition, lamivudine, marketed by ViiV, competes with emtricitabine, the active pharmaceutical ingredient of Emtriva and a component of Genvoya, Stribild, Complera/Eviplera, Atripla and Truvada. For Tybost, we compete with ritonavir marketed by AbbVie.

We also face competition from generic HIV products. Generic versions of lamivudine and Combivir (lamivudine and zidovudine) are available in the United States and certain other countries. Generic versions of Sustiva (efavirenz), a component of our Atripla, are now available in Canada and Europe and we anticipate competition from generic efavirenz in the United States in December 2017. We have observed some pricing pressure related to the Sustiva component of our Atripla sales.

Our HBV products, Viread and Hepsera, face competition from Baraclude (entecavir) marketed by BMS as well as generic entecavir. Our HBV products also compete with Tyzeka/Sebivo (telbivudine) marketed by Novartis Pharmaceuticals Corporation (Novartis).

Zydelig competes with Imbruvica (ibrutinib) marketed by Pharmacyclics LLC (an AbbVie company), Gazyva (obinutuzumab) marketed by Genentech (a member of the Roche Group) and Treanda (bendamustine hydrochloride) marketed by Cephalon, Inc.

Letairis competes with Tracleer (bosentan) and Opsumit (macitentan) marketed by Actelion Pharmaceuticals US, Inc. and also with Adcirca (tadalafil) marketed by United Therapeutics Corporation and Pfizer Inc. (Pfizer).

Ranexa competes predominantly with generic compounds from three distinct classes of drugs for the treatment of chronic angina in the United States, including generic and/or branded beta-blockers, calcium channel blockers and long-acting nitrates.

Cayston competes with Tobi (tobramycin inhalation solution) marketed by Novartis.
Tamiflu competes with Relenza (zanamivir) marketed by GlaxoSmithKline (GSK) and products sold by generic competitors.
AmBisome competes with Vfend (voriconazole) marketed by Pfizer and caspofungin, a product developed by Merck that is marketed as Cancidas in the United States and as Caspofungin elsewhere. In addition, we are aware of at least three lipid formulations that claim similarity to AmBisome becoming available outside of the United States. These formulations may reduce market demand for AmBisome. Furthermore, the manufacture of lipid formulations of amphotericin B is very complex and if any of these formulations are found to be unsafe, sales of AmBisome may be negatively impacted by association.
In addition, a number of companies are pursuing the development of technologies which are competitive with our existing products or research programs. These competing companies include specialized pharmaceutical firms and large pharmaceutical companies acting either independently or together with other pharmaceutical companies. Furthermore, academic institutions, government agencies and other public and private organizations conducting research may seek patent protection and may establish collaborative arrangements for competitive products or programs. If any of these competitors gain market share on our products, it could adversely affect our results of operations and stock price.
If significant safety issues arise for our marketed products or our product candidates, our future sales may be reduced, which would adversely affect our results of operations.
The data supporting the marketing approvals for our products and forming the basis for the safety warnings in our product labels were obtained in controlled clinical trials of limited duration and, in some cases, from post-approval use. As our products are used over longer periods of time by many patients with underlying health problems, taking numerous other medicines, we expect to continue to find new issues such as safety, resistance or drug interaction issues, which may require us to provide additional warnings or contraindications on our labels or narrow our approved indications, each of which could reduce the market acceptance of these products.
Regulatory authorities have been moving towards more active and transparent pharmacovigilance and are making greater amounts of stand-alone safety information and clinical trial data directly available to the public through websites and other means, e.g. periodic safety update report summaries, risk management plan summaries and various adverse event data. Safety information, without the appropriate context and expertise, may be misinterpreted and lead to misperception or legal action which may potentially cause our product sales or stock price to decline. Further, if serious safety, resistance or drug interaction issues arise with our marketed products, sales of these products could be limited or halted by us or by regulatory authorities and our results of operations would be adversely affected.
Our operations depend on compliance with complex FDA and comparable international regulations. Failure to obtain broad approvals on a timely basis or to maintain compliance could delay or halt commercialization of our products.
The products we develop must be approved for marketing and sale by regulatory authorities and, once approved, are subject to extensive regulation by the U.S. Food and Drug Administration (FDA), the European Medicines Agency (EMA) and comparable regulatory agencies in other countries. We are continuing clinical trials for Harvoni, Sovaldi, Epclusa, Truvada, Atripla, Stribild, Complera/Eviplera, Viread, Genvoya, Descovy, Odefsey, Emtriva, Tybost, Vitekta, Letairis, Ranexa, Cayston, Zydelig and Hepsera for currently approved and additional uses. We anticipate that we will file for marketing approval in additional countries and for additional indications and products over the next several years. These products may fail to receive such marketing approvals on a timely basis, or at all.
Further, how we manufacture and sell our products is subject to extensive regulation and review. Discovery of previously unknown problems with our marketed products or problems with our manufacturing, safety reporting or promotional activities may result in restrictions on our products, including withdrawal of the products from the market. If we fail to comply with applicable regulatory requirements, including those related to promotion and manufacturing, we could be subject to penalties including fines, suspensions of regulatory approvals, product recalls, seizure of products and criminal prosecution.
For example, under FDA rules, we are often required to conduct post-approval clinical studies to assess a known serious risk, signals of serious risk or to identify an unexpected serious risk and implement a Risk Evaluation and

Mitigation Strategy for our products, which could include a medication guide, patient package insert, a communication plan to healthcare providers or other elements as FDA deems are necessary to assure safe use of the drug, which could include imposing certain restrictions on the distribution or use of a product. Failure to comply with these or other requirements, if imposed on a sponsor by FDA, could result in significant civil monetary penalties and our operating results may be adversely affected.

The results and anticipated timelines of our clinical trials are uncertain and may not support continued development of a product candidate, which would adversely affect our prospects for future revenue growth.

We are required to demonstrate the safety and efficacy of products that we develop for each intended use through extensive preclinical studies and clinical trials. The results from preclinical and early clinical studies do not always accurately predict results in later, large-scale clinical trials. Even successfully completed large-scale clinical trials may not result in marketable products. For example, in January 2016, we announced that we terminated our Phase 2 trial of simtuzumab for the treatment of idiopathic pulmonary fibrosis after results showed a lack of treatment benefit. If any of our product candidates fails to achieve its primary endpoint in clinical trials, if safety issues arise or if the results from our clinical trials are otherwise inadequate to support regulatory approval of our product candidates, commercialization of that product candidate could be delayed or halted. In addition, we may also face challenges in clinical trial protocol design.

If the clinical trials for any of the product candidates in our pipeline are delayed or terminated, our prospects for future revenue growth would be adversely impacted. For example, we face numerous risks and uncertainties with our product candidates, including the single-tablet regimen of bictegravir (formerly GS-9883), emtricitabine and TAF, the single-tablet regimen of sofosbuvir, velpatasvir and voxilaprevir (formerly GS-9857) for the treatment of chronic HCV, idelalisib for the treatment of relapsed refractory chronic lymphocytic leukemia; momelotinib for the treatment of myelofibrosis; eleclazine for the treatment of long QT-3 syndrome; and GS-5745 for the treatment of ulcerative colitis and gastric cancer, each currently in Phase 3 clinical trials, that could prevent completion of development of these product candidates. These risks include our ability to enroll patients in clinical trials, the possibility of unfavorable results of our clinical trials, the need to modify or delay our clinical trials or to perform additional trials and the risk of failing to obtain FDA and other regulatory body approvals. As a result, our product candidates may never be successfully commercialized. Further, we may make a strategic decision to discontinue development of our product candidates if, for example, we believe commercialization will be difficult relative to other opportunities in our pipeline. If these programs and others in our pipeline cannot be completed on a timely basis or at all, then our prospects for future revenue growth may be adversely impacted. In addition, clinical trials involving our commercial products could raise new safety issues for our existing products, which could in turn decrease our revenues and harm our business.

Due to our reliance on third-party contract research organizations to conduct our clinical trials, we are unable to directly control the timing, conduct, expense and quality of our clinical trials.

We extensively outsource our clinical trial activities and usually perform only a small portion of the start-up activities in-house. We rely on independent third-party contract research organizations (CROs) to perform most of our clinical studies, including document preparation, site identification, screening and preparation, pre-study visits, training, program management and bioanalytical analysis. Many important aspects of the services performed for us by the CROs are out of our direct control. If there is any dispute or disruption in our relationship with our CROs, our clinical trials may be delayed. Moreover, in our regulatory submissions, we rely on the quality and validity of the clinical work performed by third-party CROs. If any of our CROs' processes, methodologies or results were determined to be invalid or inadequate, our own clinical data and results and related regulatory approvals could be adversely affected.

We depend on relationships with other companies for sales and marketing performance, development and commercialization of product candidates and revenues. Failure to maintain these relationships, poor performance by these companies or disputes with these companies could negatively impact our business.

We rely on a number of significant collaborative relationships with major pharmaceutical companies for our sales and marketing performance in certain territories. These include collaborations with Janssen for Odefsey and Complera/Eviplera; BMS for Atripla in the United States, Europe and Canada; F. Hoffmann-La Roche Ltd. (together with Hoffmann-La Roche Inc., Roche) for Tamiflu worldwide; and GSK for ambrisentan in territories outside of the United States. In some countries, we rely on international distributors for sales of Truvada, Viread, Hepsera, Emtriva and AmBisome. Some of these relationships also involve the clinical development of these products by our partners. Reliance on collaborative relationships poses a number of risks, including the risk that:

- we are unable to control the resources our corporate partners devote to our programs or products;
- disputes may arise with respect to the ownership of rights to technology developed with our corporate partners;

- disagreements with our corporate partners could cause delays in, or termination of, the research, development or commercialization of product candidates or result in litigation or arbitration;
- contracts with our corporate partners may fail to provide significant protection or may fail to be effectively enforced if one of these partners fails to perform;
- our corporate partners have considerable discretion in electing whether to pursue the development of any additional products and may pursue alternative technologies or products either on their own or in collaboration with our competitors;

- our corporate partners with marketing rights may choose to pursue competing technologies or to devote fewer resources to the marketing of our products than they do to products of their own development; and
- our distributors and our corporate partners may be unable to pay us, particularly in light of current economic conditions.

Given these risks, there is a great deal of uncertainty regarding the success of our current and future collaborative efforts. If these efforts fail, our product development or commercialization of new products could be delayed or revenues from products could decline.

In addition, Letairis and Cayston are distributed through third-party specialty pharmacies, which are pharmacies specializing in the dispensing of medications for complex or chronic conditions that may require a high level of patient education and ongoing counseling. The use of specialty pharmacies requires significant coordination with our sales and marketing, medical affairs, regulatory affairs, legal and finance organizations and involves risks, including but not limited to risks that these specialty pharmacies will:

- not provide us with accurate or timely information regarding their inventories, patient data or safety complaints;
- not effectively sell or support Letairis or Cayston;
- not devote the resources necessary to sell Letairis or Cayston in the volumes and within the time frames that we expect;
- not be able to satisfy their financial obligations to us or others; or
- cease operations.

We also rely on a third party to administer our Letairis Education and Access Program (LEAP), the restricted distribution program designed to support Letairis. This third party provides information and education to prescribers and patients on the risks of Letairis, confirms insurance coverage and investigates alternative sources of reimbursement or assistance, ensures fulfillment of the risk management requirements mandated for Letairis by FDA and coordinates and controls dispensing to patients through the third-party specialty pharmacies. Failure of this third party or the specialty pharmacies that distribute Letairis to perform as expected may result in regulatory action from FDA or decreased Letairis sales, either of which would harm our business.

Further, Cayston may only be taken by patients using a specific inhalation device that delivers the drug to the lungs of patients. Our ongoing distribution of Cayston is entirely reliant upon the manufacturer of that device. This manufacturer could encounter other issues with regulatory agencies related to the device or be unable to supply sufficient quantities of this device. In addition, the manufacturer may not be able to provide adequate warranty support for the device after it has been distributed to patients. With respect to distribution of the drug and device to patients, we are reliant on the capabilities of specialty pharmacies. For example, the distribution channel for drug and device is complicated and requires coordination. The reimbursement approval processes associated with both drug and device are similarly complex. If the device manufacturer is unable to obtain reimbursement approval or receives approval at a lower-than-expected price, sales of Cayston may be adversely affected. Any of the previously described issues may limit the sales of Cayston, which would adversely affect our financial results.

Our success will depend to a significant degree on our ability to defend our patents and other intellectual property rights both domestically and internationally. We may not be able to obtain effective patents to protect our technologies from use by competitors and patents of other companies could require us to stop using or pay for the use of required technology.

Patents and other proprietary rights are very important to our business. Our success will depend to a significant degree on our ability to:

- obtain patents and licenses to patent rights;
- preserve trade secrets;
- defend against infringement and efforts to invalidate our patents; and
- operate without infringing on the intellectual property of others.

If we have a properly drafted and enforceable patent, it can be more difficult for our competitors to use our technology to create competitive products and more difficult for our competitors to obtain a patent that prevents us from using technology we create. As part of our business strategy, we actively seek patent protection both in the United States and internationally and file additional patent applications, when appropriate, to cover improvements in

our compounds, products and technology.

We have a number of U.S. and foreign patents, patent applications and rights to patents related to our compounds, products and technology, but we cannot be certain that issued patents will be enforceable or provide adequate protection or that pending patent applications will result in issued patents. Patent applications are confidential for a period of time before a patent is issued. As a result, we may not know if our competitors filed patent applications for technology covered by our pending applications or if we were the first to invent or first to file an application directed toward the technology that is the subject of our patent applications. Competitors may have filed patent applications or received patents and may obtain additional patents and proprietary rights that

block or compete with our products. In addition, if competitors file patent applications covering our technology, we may have to participate in litigation, interference or other proceedings to determine the right to a patent. Litigation, interference or other proceedings are unpredictable and expensive, such that, even if we are ultimately successful, our results of operations may be adversely affected by such events.

Tenofovir disoproxil fumarate, one of the active pharmaceutical ingredients in Stribild, Complera/Eviplera, Atripla and Truvada, is expected to face generic competition in the United States and European Union in 2017, which may have an impact on our business and results of operations. In addition, patents do not cover the ranolazine compound, the active ingredient of Ranexa. Instead, when it was discovered that only a sustained-release formulation of ranolazine would achieve therapeutic plasma levels, patents were obtained on those formulations and the characteristic plasma levels they achieve. Patents do not cover the active ingredients in AmBisome.

We may obtain patents for certain products many years before marketing approval is obtained for those products. Because patents have a limited life, which may begin to run prior to the commercial sale of the related product, the commercial value of the patent may be limited. However, we may be able to apply for patent term extensions or supplementary protection certificates in some countries.

Generic manufacturers have sought, and may continue to seek, FDA approval to market generic versions of our products through an abbreviated new drug application (ANDA), the application form typically used by manufacturers seeking approval of a generic drug. See a description of our ANDA litigation in Note 10 Commitments and Contingencies of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q and risk factor entitled "Litigation with generic manufacturers has increased our expenses which may continue to reduce our earnings. If we are unsuccessful in all or some of these lawsuits, some or all of our claims in the patents may be narrowed or invalidated and generic versions of our products could be launched prior to our patent expiry." beginning on page 49.

Our success depends in large part on our ability to operate without infringing upon the patents or other proprietary rights of third parties.

If we infringe the valid patents of third parties, we may be prevented from commercializing products or may be required to obtain licenses from these third parties. We may not be able to obtain alternative technologies or any required license on reasonable terms or at all. If we fail to obtain these licenses or alternative technologies, we may be unable to develop or commercialize some or all of our products. For example, we are aware of patents that may relate to our operation of LEAP, our restricted distribution program designed to support Letairis and we are aware of patents and patent applications owned by other parties that may claim to cover the use of sofosbuvir. See a description of our litigation regarding sofosbuvir in Note 10 Commitments and Contingencies of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q and the risk factor entitled "If any party is successful in establishing exclusive rights to Harvoni, Sovaldi and/or Epclusa, our expected revenues and earnings from the sale of Harvoni, Sovaldi and/or Epclusa could be adversely affected" beginning on page 45.

Furthermore, we also rely on unpatented trade secrets and improvements, unpatented internal know-how and technological innovation. We protect these rights mainly through confidentiality agreements with our corporate partners, employees, consultants and vendors. These agreements provide that all confidential information developed or made known to an individual during the course of their relationship with us will be kept confidential and will not be used or disclosed to third parties except in specified circumstances. In the case of employees, the agreements provide that all inventions made by an individual while employed by us will be our exclusive property. We cannot be certain that these parties will comply with these confidentiality agreements, that we have adequate remedies for any breach or that our trade secrets will not otherwise become known or be independently discovered by our competitors. Under some of our R&D agreements, inventions become jointly owned by us and our corporate partner and in other cases become the exclusive property of one party. In certain circumstances, it can be difficult to determine who owns a particular invention and disputes could arise regarding those inventions. If our trade secrets or confidential information become known or independently discovered by competitors or if we enter into disputes over ownership of inventions, our business and results of operations could be adversely affected.

If any party is successful in establishing exclusive rights to Harvoni, Sovaldi and/or Epclusa, our expected revenues and earnings from the sale of Harvoni, Sovaldi and/or Epclusa could be adversely affected.

We own patents and patent applications that claim sofosbuvir (Sovaldi) as a chemical entity and its metabolites and the fixed-dose combinations of ledipasvir and sofosbuvir (Harvoni) and sofosbuvir and velpatasvir (Epclusa). Third parties may have, or may obtain rights to, patents that allegedly could be used to prevent or attempt to prevent us from commercializing Harvoni, Sovaldi or Epclusa. For example, we are aware of patents and patent applications owned by other parties that may be alleged by such parties to cover the use of Harvoni, Sovaldi and Epclusa. We cannot predict the ultimate outcome of intellectual property claims related to Harvoni, Sovaldi or Epclusa, and we have spent, and will continue to spend, significant resources defending against these claims. If these parties successfully obtain valid and enforceable patents, and successfully prove infringement of

those patents by Harvoni, Sovaldi and/or Epclusa, we could be prevented from selling sofosbuvir unless we were able to obtain a license under such patents. Such a license may not be available on commercially reasonable terms or at all.

Interference Proceedings and Litigation with Idenix Pharmaceuticals, Inc. (Idenix)

In February 2012, we received notice that the U.S. Patent and Trademark Office (USPTO) had declared Interference No. 105,871 (First Idenix Interference) between our U.S. Patent No. 7,429,572 (the ’572 patent) and Idenix’s pending U.S. Patent Application No. 12/131,868. An interference is a proceeding before the USPTO designed to determine who was the first to invent the subject matter claimed by both parties. In January 2014, the USPTO Patent Trial and Appeal Board (PTAB) determined that Pharmasset and not Idenix was the first to invent the compounds in dispute and accordingly we prevailed in the First Idenix Interference. Idenix has appealed the PTAB’s decisions to the U.S. District Court for the District of Delaware.

In December 2013, after receiving our request to do so, the USPTO declared Interference No. 105,981 (Second Idenix Interference) between our pending U.S. Patent Application No. 11/854,218 and Idenix’s U.S. Patent No. 7,608,600 (the ’600 patent). The ’600 patent is related to the Idenix patent application at issue in the First Idenix Interference and includes claims directed to methods of treating HCV with nucleoside compounds. The purpose of the Second Idenix Interference was to determine who was first to invent the claimed methods of treating HCV with compounds similar to those which were involved in the First Idenix Interference. In March 2015, the PTAB determined that Pharmasset and not Idenix was the first to invent the claimed methods of treating HCV. Idenix appealed this decision in both the U.S. District Court for the District of Delaware and the U.S. Court of Appeal for the Federal Circuit (CAFC). We have filed a motion to dismiss the appeal in Delaware and have responded to the appeal filed in the CAFC. The CAFC has not yet set a hearing date for this appeal. The Delaware court has stayed the appeal relating to the Second Idenix Interference.

We believe that the Idenix claims involved in the First and Second Idenix Interferences, and similar U.S. and foreign patents claiming the same compounds, metabolites and uses thereof, are invalid. As a result, we filed an Impeachment Action in the Federal Court of Canada to invalidate Idenix Canadian Patent No. 2,490,191 (the ’191 patent), which is the Canadian patent that corresponds to the ’600 patent. Idenix asserted that the commercialization of Sovaldi in Canada will infringe its ’191 patent and that our Canadian Patent No. 2,527,657, corresponding to the ’572 patent involved in the First Idenix Interference, is invalid. In November 2015, the Canadian court held that Idenix’s patent is invalid and that Gilead’s patent is valid. Idenix appealed the decision to the Canadian Federal Court of Appeal in November 2015.

We filed a similar legal action in Norway in the Oslo District Court seeking to invalidate Idenix’s Norwegian patent corresponding to the ’600 patent. In September 2013, Idenix filed an invalidation action in the Norwegian proceedings against our Norwegian Patent No. 333700 patent, which corresponds to the ’572 patent. In March 2014, the Norwegian court found all claims in the Idenix Norwegian patent to be invalid and upheld the validity of all claims in the challenged Gilead patent. Idenix appealed the decision to the Norwegian Court of Appeal. In April 2016, the Court of Appeal issued its decision invalidating the Idenix patent and upholding the Gilead patent. Idenix has not filed a further appeal.

In January 2013, we filed a legal action in the Federal Court of Australia seeking to invalidate Idenix’s Australian patent corresponding to the ’600 patent. In April 2013, Idenix asserted that the commercialization of Sovaldi in Australia infringes its Australian patent corresponding to the ’600 patent. In March 2016, the Australia court revoked Idenix’s patent. Idenix has appealed this decision. The appeal hearing is scheduled for November 2016.

In March 2014, the European Patent Office (EPO) granted Idenix European Patent No. 1 523 489 (the ’489 patent), which corresponds to the ’600 patent. The same day that the ’489 patent was granted, we filed an opposition with the EPO seeking to revoke the ’489 patent. An opposition hearing was held in February 2016, and the EPO ruled in our favor and revoked the ’489 patent. In March 2014, Idenix also initiated infringement proceedings against us in the United Kingdom (UK), Germany and France alleging that the commercialization of Sovaldi would infringe the UK, German and French counterparts of the ’489 patent. A trial was held in the UK in October 2014 to determine the issues of infringement and validity of the Idenix UK patent. In December 2014, the High Court of Justice of England and Wales (UK Court) invalidated all challenged claims of the ’489 patent on multiple grounds. Idenix appealed. The

appeal hearing was held in July 2016. In March 2015, the German court in Düsseldorf determined that the Idenix patent was highly likely to be invalid and stayed the infringement proceedings pending the outcome of the opposition hearing held by the EPO in February 2016. Idenix has not appealed this decision of the German court staying the proceedings. Upon Idenix's request, the French proceedings have been stayed; however, in March 2016, Idenix requested that the French litigation be reactivated.

Idenix has not been awarded patents corresponding to the '600 patent in Japan or China. In the event such patents are issued, we expect to challenge them in proceedings similar to those we invoked in other countries.

In December 2013, Idenix, Universita Degli Studi di Cagliari (UDSG), Centre National de la Recherche Scientifique and L'Université Montpellier II sued us in U.S. District Court for the District of Delaware alleging that the commercialization of

sofosbuvir will infringe the ’600 patent and that an interference exists between the ’600 patent and our U.S. Patent No. 8,415,322. Also in December 2013, Idenix and UDSG sued us in the U.S. District Court for the District of Massachusetts alleging that the commercialization of sofosbuvir will infringe U.S. Patent Nos. 6,914,054 and 7,608,597. In June 2014, the court transferred the Massachusetts litigation to the U.S. District Court for the District of Delaware. The Delaware district court has set trial dates in October 2016 and December 2016 for resolution of these issues. A decision by the district court may be appealed by either party to the CAFC.

Idenix was acquired by Merck & Co. Inc. (Merck) in August 2014, and Merck continues to pursue the Idenix claims described herein.

Litigation with Merck

In August 2013, Merck contacted us requesting that we pay royalties on the sales of sofosbuvir and obtain a license to U.S. Patent No. 7,105,499 (the ’499 patent) and U.S. Patent No. 8,481,712 (the ’712 patent), which it co-owns with Isis Pharmaceuticals, Inc. The ’499 and ’712 patents cover compounds which do not include, but may relate to, sofosbuvir. We filed a lawsuit in August 2013 in the U.S. District Court for the Northern District of California seeking a declaratory judgment that the Merck patents are invalid and not infringed. During patent prosecution, Merck amended its patent application in an attempt to cover compounds related to sofosbuvir. Initially, in March 2016, a jury determined that we had not established that Merck’s patents are invalid for lack of written description or lack of enablement and awarded Merck $200 million in damages. However, in June 2016, the court ruled in our favor on our defense of unclean hands. As a result, the court determined that Merck may not recover any damages from us for the ’499 and ’712 patents. We have filed a motion seeking recovery of certain fees and have requested judgment that the jury’s earlier verdict should be vacated. Once the court has heard and ruled on our motions, the case will be ready for appeal. Merck has filed a notice of appeal to the Court of Appeals for the Federal Circuit regarding the court’s decision on our defense of unclean hands.

If the decision on our defense of unclean hands is reversed on appeal, we may be required to pay damages and a royalty on sales of sofosbuvir-containing products following the appeal. In that event, the judge has indicated that she will determine the amount of the royalty, if necessary, at the conclusion of any appeal in this case.

Litigation with AbbVie

AbbVie has obtained U.S. Patent Nos. 8,466,159, 8,492,386, 8,680,106, 8,685,984, and 8,809,265 (the AbbVie Patents) which purport to cover the use of a combination of LDV/SOF (or Harvoni) for the treatment of HCV. We are aware that AbbVie has pending patent applications in the United States and granted and pending applications in other countries. We own published and pending patent applications directed to the use of combinations for the treatment of HCV, and, specifically, to the combination of LDV/SOF. Certain of our applications were filed before the AbbVie Patents. For this reason and others, we believe the AbbVie Patents are invalid.

Accordingly, in December 2013, we filed a lawsuit in the U.S. District Court for the District of Delaware seeking declaratory judgment that the AbbVie Patents are invalid and unenforceable, as well as other relief. We believe that Abbott Laboratories, Inc. and AbbVie conspired to eliminate competition in the HCV market by falsely representing to the USPTO that they, and not Gilead, invented methods of treating HCV using a combination of LDV/SOF. In February and March 2014, AbbVie responded to our lawsuit by also filing two lawsuits in the U.S. District Court for the District of Delaware alleging that our fixed-dose combination of LDV/SOF will infringe its patents. All of those lawsuits have been consolidated into a single action. In the United States, either party may appeal a decision by the District Court to the CAFC. The AbbVie Patents have not blocked or delayed the commercialization of our combination products in the United States, Canada, or Europe. We do not expect any other foreign patents to block or delay the commercialization around the world. The court has set a trial date of September 12, 2016 for this lawsuit.

Additionally, AbbVie has obtained U.S. Patent No. 9,034,832 which purports to cover a solid oral dosage form containing ledipasvir. Accordingly, in May 2015, we filed a lawsuit in the U.S. District Court for the District of Delaware seeking declaratory judgment that AbbVie’s patent is invalid, as well as other relief. The AbbVie Patents have not blocked the commercialization of our combination products. The court has set a trial date of July 31, 2017 for this lawsuit.

In August 2015, we filed an impeachment action against AbbVie seeking a declaration that AbbVie’s Canadian Patent No. 2,811,250 (the ’250 patent), which purports to cover the use of a combination of LDV/SOF for the treatment of

HCV, is invalid. On the same day, AbbVie filed an infringement action against us asserting that commercialization of Harvoni in Canada will infringe the ’250 patent. The impeachment action has been stayed and we have counterclaimed for invalidity in the infringement proceeding. The court has set a trial date of April 11, 2018 for this impeachment action.

Additionally, AbbVie has obtained Canadian Patent No. 2,857,339 (the ’339 patent) which purports to cover a solid composition that contains ledipasvir. In November 2015, AbbVie filed an infringement action against us asserting that

commercialization of Harvoni in Canada infringes the ’339 patent. We have filed a counterclaim asserting the invalidity of AbbVie’s patent. The court has set a trial date of October 15, 2018 for this impeachment action.

In November 2015, AbbVie filed a lawsuit against us in the Regional Court Düsseldorf for infringement of two quasi-patents, known as "utility models." Utility models are unexamined IP rights and are not the same as standard patents. One utility model, DE 20 2012 013 117, purports to cover the use of a combination of direct-acting antivirals which includes at least an HCV polymerase inhibitor and an HCV NS5A inhibitor in the treatment of HCV; the other utility model, DE 21 2012 000 197, purports to cover a solid dispersion that includes ledipasvir. The court has set a trial date of March 23, 2017 for this lawsuit.

European Patent Claims

In February 2015, several parties filed oppositions in the EPO requesting revocation of our granted European patent covering sofosbuvir that expires in 2028. In January 2016, several parties filed oppositions in the EPO requesting revocation of our granted European patent covering TAF that expires in 2021. In March 2016, three parties filed oppositions in the EPO requesting revocation of our granted European patent covering cobicistat that expires in 2027. While we are confident in the strength of our patents, we cannot predict the ultimate outcome of these actions. If we are unsuccessful in defending these oppositions, some or all of our patent claims may be narrowed or revoked and the patent protection for sofosbuvir, TAF and cobicistat in Europe could be substantially shortened or eliminated entirely. If our patents are revoked, and no other European patents are granted covering these compounds, our exclusivity may be based entirely on regulatory exclusivity granted by the EMA. Sovaldi has been granted regulatory exclusivity that will prevent generic sofosbuvir from entering the European Union for 10 years following approval of Sovaldi, or January 2024. If we lose exclusivity for Sovaldi prior to 2028, our expected revenues and results of operation could be negatively impacted for the years including and succeeding the year in which such exclusivity is lost, which may cause our stock price to decline.

Manufacturing problems, including at our third-party manufacturers and corporate partners, could cause inventory shortages and delay product shipments and regulatory approvals, which may adversely affect our results of operations.

In order to generate revenue from our products, we must be able to produce sufficient quantities of our products to satisfy demand. Many of our products are the result of complex manufacturing processes. The manufacturing process for pharmaceutical products is also highly regulated and regulators may shut down manufacturing facilities that they believe do not comply with regulations.

Our products are either manufactured at our own facilities or by third-party manufacturers or corporate partners. We depend on third parties to perform manufacturing activities effectively and on a timely basis for the majority of our solid dose products. In addition, Roche, either by itself or through third parties, is responsible for manufacturing Tamiflu. We, our third-party manufacturers and our corporate partners are subject to Good Manufacturing Practices (GMP), which are extensive regulations governing manufacturing processes, stability testing, record keeping and quality standards as defined by FDA and the EMA. Similar regulations are in effect in other countries.

Our third-party manufacturers and corporate partners are independent entities who are subject to their own unique operational and financial risks which are out of our control. If we or any of these third-party manufacturers or corporate partners fail to perform as required, this could impair our ability to deliver our products on a timely basis or receive royalties or cause delays in our clinical trials and applications for regulatory approval. Further, we may have to write-off the costs of manufacturing any batch that fails to pass quality inspection or meet regulatory approval. In addition, we, our third-party manufacturers and our corporate partners may only be able to produce some of our products at one or a limited number of facilities and, therefore, have limited manufacturing capacity for certain products. To the extent these risks materialize and affect their performance obligations to us, our financial results may be adversely affected.

Our manufacturing operations are subject to routine inspections by regulatory agencies. If we are unable to remedy any deficiencies cited by FDA in these inspections, our currently marketed products and the timing of regulatory approval of products in development could be adversely affected. Further, there is risk that regulatory agencies in other countries where marketing applications are pending will undertake similar additional reviews or apply a heightened standard of review, which could delay the regulatory approvals for products in those countries. If

approval of any of our product candidates were delayed or if production of our marketed products was interrupted, our anticipated revenues and our stock price would be adversely affected.

We may not be able to obtain materials or supplies necessary to conduct clinical trials or to manufacture and sell our products, which would limit our ability to generate revenues.

We need access to certain supplies and products to conduct our clinical trials and to manufacture our products. If we are unable to purchase sufficient quantities of these materials or find suitable alternate materials in a timely manner, our development efforts for our product candidates may be delayed or our ability to manufacture our products would be limited, which would limit our ability to generate revenues.

Suppliers of key components and materials must be named in the NDA or MAA filed with FDA, EMA or other regulatory authority for any product candidate for which we are seeking marketing approval, and significant delays can occur if the qualification of a new supplier is required. Even after a manufacturer is qualified by the regulatory authority, the manufacturer must continue to expend time, money and effort in the area of production and quality control to ensure full compliance with GMP. Manufacturers are subject to regular, periodic inspections by the regulatory authorities following initial approval. If, as a result of these inspections, a regulatory authority determines that the equipment, facilities, laboratories or processes do not comply with applicable regulations and conditions of product approval, the regulatory authority may suspend the manufacturing operations. If the manufacturing operations of any of the single suppliers for our products are suspended, we may be unable to generate sufficient quantities of commercial or clinical supplies of product to meet market demand, which would in turn decrease our revenues and harm our business. In addition, if delivery of material from our suppliers were interrupted for any reason, we may be unable to ship certain of our products for commercial supply or to supply our products in development for clinical trials. In addition, some of our products and the materials that we utilize in our operations are made at only one facility. For example, we manufacture certain drug product intermediates utilized in AmBisome exclusively at our facilities in San Dimas, California. In the event of a disaster, including an earthquake, equipment failure or other difficulty, we may be unable to replace this manufacturing capacity in a timely manner and may be unable to manufacture AmBisome to meet market needs.

In addition, we depend on a single supplier for amphotericin B, the active pharmaceutical ingredient of AmBisome, and high-quality cholesterol in the manufacture of AmBisome. We also rely on a single source for the active pharmaceutical ingredients found in Letairis and Cayston. Astellas US LLC, which markets Lexiscan in the United States, is responsible for the commercial manufacture and supply of product in the United States and is dependent on a single supplier for the active pharmaceutical ingredient of Lexiscan. Problems with any of the single suppliers we depend on may negatively impact our development and commercialization efforts.

A significant portion of the raw materials and intermediates used to manufacture our antiviral products (including Harvoni, Sovaldi, Epclusa, Truvada, Atripla, Stribild, Complera/Eviplera, Viread, Genvoya, Descovy, Odefsey and Emtriva) are supplied by China-based companies. As a result, an international trade dispute between China and the United States or any other actions by the Chinese government that would limit or prevent Chinese companies from supplying these materials would adversely affect our ability to manufacture and supply our antiviral products to meet market needs and have a material and adverse effect on our operating results.

Litigation with generic manufacturers has increased our expenses which may continue to reduce our earnings. If we are unsuccessful in all or some of these lawsuits, some or all of our claims in the patents may be narrowed or invalidated and generic versions of our products could be launched prior to our patent expiry.

As part of the approval process for some of our products, FDA granted us a New Chemical Entity (NCE) exclusivity period during which other manufacturers' applications for approval of generic versions of our product will not be approved. Generic manufacturers may challenge the patents protecting products that have been granted NCE exclusivity one year prior to the end of the NCE exclusivity period. Generic manufacturers have sought and may continue to seek FDA approval for a similar or identical drug through an ANDA, the application form typically used by manufacturers seeking approval of a generic drug. Current legal proceedings of significance with some of our generic manufacturers include:

Apotex

In June 2014, we received notice that Apotex Inc. (Apotex) submitted an abbreviated new drug submission (ANDS) to Health Canada requesting permission to manufacture and market a generic version of Truvada and a separate ANDS requesting permission to manufacture and market a generic version of Viread. In the notice, Apotex alleges that three of the patents associated with Truvada and two of the patents associated with Viread are invalid, unenforceable and/or will not be infringed by Apotex's manufacture, use or sale of a generic version of Truvada or Viread. In August 2014, we filed lawsuits against Apotex in the Federal Court of Canada seeking orders of prohibition against approval of these ANDSs. A hearing in those cases was held in April 2016. In July 2016, the court issued an order prohibiting the Canadian Minister of Health from approving Apotex's generic version of our Viread product until the expiry of our patents in July 2017. The court declined to prohibit approval of Apotex's generic version of our Truvada product. The court's decision did not rule on the validity of the patents. The launch of Apotex's generic version of our Truvada product would be at risk of infringement of our patents, including patents that we were unable to assert in the present lawsuit, and liability for our damages. Apotex may elect to appeal the decision.

Teva

In November 2011, December 2011 and August 2012, we received notices that Teva Pharmaceuticals (Teva) submitted an abbreviated new drug submission (ANDS) to the Canadian Minister of Health requesting permission to manufacture and market generic versions of Truvada, Atripla and Viread. In the notices, Teva alleges that the patents associated with Truvada, Atripla and Viread are invalid, unenforceable and/or will not be infringed by Teva's manufacture, use or sale of generic versions of those products. We filed lawsuits against Teva in the Federal Court of Canada seeking an order of prohibition against approval of these applications.

In December 2013, the court issued an order prohibiting the Canadian Minister of Health from approving Teva's generic versions of our Viread, Truvada and Atripla products until expiry of our patent in July 2017. Teva has appealed that decision. The court's decision did not rule on the validity of the patents and accordingly the only issue on appeal is whether the Canadian Minister of Health should be prohibited from approving Teva's products. The appeal will be heard by the Canadian Federal Court of Appeal after the trial in the Impeachment Action filed by Teva in August 2012 seeking invalidation of one of our Canadian patents associated with Viread. The court will determine the validity of the patent in the pending Impeachment Action. A trial in the Impeachment Action is scheduled for November 2016. If Teva is successful in invalidating the patent, Teva may be able to launch generic versions of our Viread, Truvada and Atripla products in Canada prior to the expiry of our patents.

Mylan

In February 2016, we received notice that Mylan Pharmaceuticals, Inc. (Mylan) submitted an ANDA to FDA requesting permission to manufacture and market a generic version of Tybost (cobicistat). In the notice, Mylan alleges that the patent covering cobicistat is invalid as obvious and that Mylan's generic product cannot infringe an invalid claim. In March 2016, we filed lawsuits against Mylan in the U.S. District Court for the District of Delaware and U.S. District Court for the Northern District of West Virginia. The trial in Delaware is scheduled for January 2018. The patent in suit that covers Tybost is also listed in the Orange Book for Stribild and Genvoya.

Aurobindo

In May 2016, we received notices that Aurobindo Pharma (Aurobindo) submitted ANDAs to FDA requesting permission to manufacture and market generic versions of Emtriva and Truvada. In the notices, Aurobindo alleges that two of the patents associated with our emtricitabine tablets and four of the patents associated with our emtricitabine and tenofovir disoproxil fumarate fixed dose combination tablets are invalid, unenforceable and/or will not be infringed by Aurobindo's manufacture, use or sale of generic versions of Emtriva and Truvada, respectively. In June 2016 and July 2016, we filed lawsuits against Aurobindo in the U.S. District Court for the District of New Jersey for infringement of the patents associated with Emtriva and Truvada.

Watson

In February 2015, we received notice that Watson Laboratories, Inc. (Watson) submitted an ANDA to FDA requesting permission to manufacture and market a generic version of Letairis. In the notice, Watson alleges that one of the patents associated with ambrisentan tablets is invalid, unenforceable and/or will not be infringed by Watson's manufacture, use or sale of a generic version of Letairis. In April 2015, we filed a lawsuit against Watson in the U.S.

District Court for the District of New Jersey.

SigmaPharm

In June 2015, we received notice that SigmaPharm Laboratories, LLC (SigmaPharm) submitted an ANDA to FDA requesting permission to manufacture and market a generic version of Letairis. In the notice, SigmaPharm alleges that one of the patents associated with ambrisentan tablets is invalid, unenforceable and/or will not be infringed by SigmaPharm's manufacture, use or sale of a generic version of Letairis. In June 2015, we filed a lawsuit against SigmaPharm in the U.S. District Court for the District of New Jersey.

We cannot predict the ultimate outcome of the foregoing actions and other litigation with generic manufacturers, and we may spend significant resources enforcing and defending these patents. If we are unsuccessful in these lawsuits, some or all of our original claims in the patents may be narrowed or invalidated and the patent protection for Truvada, Viread and Letairis in the United States and Atripla, Truvada and Viread in Canada could be substantially shortened. Further, if all of the patents covering one or more products are invalidated, FDA or the Canadian Minister of Health could approve the requests to manufacture a generic version of such products in the United States or Canada, respectively, prior to the expiration date of those patents. The sale of generic versions of these products earlier than their patent expiration would have a significant negative effect on our revenues and results of operations.

We face credit risks from our Emerging Market and Southern European customers that may adversely affect our results of operations.

We have exposure to customer credit risks in emerging markets and Southern Europe. Southern European product sales to government-owned or supported customers in Southern Europe, specifically Spain, Italy, Portugal and Greece have historically been subject to significant payment delays due to government funding and reimbursement practices. This has resulted and may continue to result in days sales outstanding being significantly higher in these countries due to the average length of time that accounts receivable remain outstanding. As of June 30, 2016, our accounts receivable in Southern Europe, specifically Greece, Italy, Portugal and Spain, totaled approximately $630 million, of which $171 million were greater than 120 days past due, including $36 million greater than 365 days past due.

Historically, receivable balances with certain publicly-owned hospitals accumulate over a period of time and are then subsequently settled as large lump sum payments. This pattern is also experienced by other pharmaceutical companies that sell directly to hospitals. If significant changes were to occur in the reimbursement practices of these European governments or if government funding becomes unavailable, we may not be able to collect on amounts due to us from these customers and our results of operations would be adversely affected.

Our revenues and gross margin could be reduced by imports from countries where our products are available at lower prices.

Prices for our products are based on local market economics and competition and sometimes differ from country to country. Our sales in countries with relatively higher prices may be reduced if products can be imported into those or other countries from lower price markets. There have been cases in which other pharmaceutical products were sold at steeply discounted prices in the developing world and then re-exported to European countries where they could be re-sold at much higher prices. If this happens with our products, particularly Truvada and Viread, which we have agreed to make available at substantially reduced prices to more than 125 countries participating in our Gilead Access Program, or Atripla, which Merck distributes at substantially reduced prices to HIV infected patients in developing countries under our 2006 agreement, our revenues would be adversely affected. In addition, we have established partnerships with India-based generic manufacturers to distribute generic versions of tenofovir disoproxil fumarate and TAF, contingent on U.S. regulatory approval, to 112 developing world countries, including India. We expanded these agreements to include rights to Stribild, Tybost and Vitekta. We also entered into agreements with certain India-based generic manufacturers to produce and distribute generic emtricitabine in the developing world, including single-tablet regimens containing emtricitabine and fixed-dose combinations of emtricitabine co-formulated with our other HIV medicines. Starting in September 2014, we entered into licensing agreements with India-based generic manufacturers to produce and distribute generic sofosbuvir and the fixed-dose combination of LDV/SOF to 101 developing countries. If generic versions of our HIV and HCV medications under these licenses are then re-exported to the United States, Europe or other markets outside of these developing world countries, our revenues would be adversely affected. As part of our commitment to make Sovaldi available in the developing world at discounted prices, we entered into an agreement to make Sovaldi available in Egypt, a country that has among the highest HCV prevalence in the world. If the discounted Sovaldi is re-exported from these developing countries into the United States or other higher price markets, our revenues could be adversely affected.

In addition, purchases of our products in countries where our selling prices are relatively low for resale in countries in which our selling prices are relatively high may adversely impact our revenues and gross margin and may cause our sales to fluctuate from quarter to quarter. For example, in the European Union, we are required to permit products

purchased in one country to be sold in another country. Purchases of our products in countries where our selling prices are relatively low for resale in countries in which our selling prices are relatively high can affect the inventory level held by our wholesalers and can cause the relative sales levels in the various countries to fluctuate from quarter to quarter and not reflect the actual consumer demand in any given quarter. These quarterly fluctuations may impact our earnings, which could adversely affect our stock price and harm our business.

Expensive litigation and government investigations have increased our expenses which may continue to reduce our earnings.

We are involved in a number of litigation, investigation and other dispute-related matters that require us to expend substantial internal and financial resources. We expect these matters will continue to require a high level of internal and financial resources for the foreseeable future. These matters have reduced and will continue to reduce our earnings. Please see a description of our litigation, investigation and other dispute-related matters in Note 10 Commitments and Contingencies of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q. The outcome of such lawsuits or any other lawsuits that may be brought against us, the investigations or any other investigations that may be initiated, are inherently uncertain, and adverse developments or outcomes can result in significant expenses, monetary damages, penalties or injunctive relief against us that could significantly reduce our earnings and cash flows and harm our business.

In some countries, we may be required to grant compulsory licenses for our products or our patents may not be enforced.

In a number of developing countries, government officials and other interested groups have suggested that pharmaceutical companies should make drugs for HCV or HIV infection available at low cost. Alternatively, governments in those developing countries could require that we grant compulsory licenses to allow competitors to manufacture and sell their own versions of our products, thereby reducing our product sales. For example, there is growing attention on the availability of HCV therapies and some activists are advocating for the increased availability of HCV therapies through means including compulsory licenses. In the past, certain offices of the government of Brazil have expressed concern over the affordability of our HIV products and declared that they were considering issuing compulsory licenses to permit the manufacture of otherwise patented products for HIV infection, including Viread. In addition, concerns over the cost and availability of Tamiflu related to a potential avian flu pandemic and H1N1 influenza generated international discussions over compulsory licensing of our Tamiflu patents. For example, the Canadian government considered allowing Canadian manufacturers to manufacture and export the active ingredient in Tamiflu to eligible developing and least developed countries under Canada's Access to Medicines Regime. Furthermore, Roche issued voluntary licenses to permit third-party manufacturing of Tamiflu. For example, Roche granted a sublicense to Shanghai Pharmaceutical (Group) Co., Ltd. for China and a sublicense to India's Hetero Drugs Limited for India and certain developing countries. If compulsory licenses permit generic manufacturing to override our product patents for Harvoni, Sovaldi, our HIV products or Tamiflu, or if we are required to grant compulsory licenses for these products, it could reduce our earnings and cash flows and harm our business.

In addition, certain countries do not permit enforcement of our patents, and third-party manufacturers are able to sell generic versions of our products in those countries. For example, in July 2009, the Brazilian patent authority rejected our patent application for tenofovir disoproxil fumarate, the active pharmaceutical ingredient in Viread. This was the highest level of appeal available to us within the Brazilian patent authority. Because we do not currently have a patent in Brazil, the Brazilian government now purchases its supply of tenofovir disoproxil fumarate from generic manufacturers. Sales of generic versions of our products could significantly reduce our sales and adversely affect our results of operations, particularly if generic versions of our products are imported into territories where we have existing commercial sales.

We may face significant liability resulting from our products that may not be covered by insurance and successful claims could materially reduce our earnings.

The testing, manufacturing, marketing and use of our commercial products, as well as product candidates in development, involve substantial risk of product liability claims. These claims may be made directly by consumers, healthcare providers, pharmaceutical companies or others. We may be unable to maintain sufficient coverage for product liabilities that may arise. In addition, the cost to defend lawsuits or pay damages for product liability claims may exceed our coverage. If we are unable to maintain adequate coverage or if claims exceed our coverage, our financial condition and our ability to clinically test our product candidates and market our products will be adversely affected. In addition, negative publicity associated with any claims, regardless of their merit, may decrease the future demand for our products and impair our financial condition.

Business disruptions from natural or man-made disasters may harm our future revenues.

Our worldwide operations could be subject to business interruptions stemming from natural or man-made disasters for which we may be self-insured. Our corporate headquarters and Fremont locations, which together house a majority of our R&D activities, and our La Verne, San Dimas and Oceanside manufacturing facilities are located in California, a seismically active region. As we may not carry adequate earthquake insurance and significant recovery time could be required to resume operations, our financial condition and operating results could be materially adversely affected in the event of a major earthquake.

We are dependent on information technology systems, infrastructure and data.

We are dependent upon information technology systems, infrastructure and data. The multitude and complexity of our computer systems make them inherently vulnerable to service interruption or destruction, malicious intrusion and random attack.

Likewise, data privacy or security breaches by employees or others may pose a risk that sensitive data, including our intellectual property, trade secrets or personal information of our employees, patients, customers or other business partners may be exposed to unauthorized persons or to the public. Cyberattacks are increasing in their frequency, sophistication and intensity. Cyberattacks could include the deployment of harmful malware, denial-of-service, social engineering and other means to affect service reliability and threaten data confidentiality, integrity and availability. Our business partners face similar risks and any security breach of their systems could adversely affect our security posture. While we have invested, and continue to invest, in the protection of our data and information technology infrastructure, there can be no assurance that our efforts will prevent service interruptions, or identify breaches in our systems, that could adversely affect our business and operations and/or result in the loss of critical or sensitive information, which could result in financial, legal, business or reputational harm to us. In addition, our liability insurance may not be sufficient in type or amount to cover us against claims related to security breaches, cyberattacks and other related breaches.

Changes in our effective income tax rate could reduce our earnings.

We are subject to income taxes in both the United States and various foreign jurisdictions including Ireland. Due to economic and political conditions, various countries are actively considering changes to existing tax laws. We cannot predict the form or timing of potential legislative changes that could have a material adverse impact on our results of operations. In addition, significant judgment is required in determining our worldwide provision for income taxes. Various factors may have favorable or unfavorable effects on our income tax rate including, but not limited to, changes in forecasted demand for our HCV products, our portion of the non-tax deductible annual BPD fee, the accounting for stock options and other share-based awards, mergers and acquisitions, the ability to manufacture product in our Cork, Ireland facility, the amortization of certain acquisition related intangibles for which we receive no tax benefit, future levels of R&D spending, changes in the mix of earnings in the various tax jurisdictions in which we operate, changes in overall levels of pre-tax earnings and resolution of federal, state and foreign income tax audits. The impact on our income tax provision resulting from the above mentioned factors may be significant and could have a negative impact on our consolidated results of operations.

Our income tax returns are subject to audit by federal, state and foreign tax authorities. We are currently under examination by the IRS for the 2010, 2011 and 2012 tax years and by various state and foreign jurisdictions. There are differing interpretations of tax laws and regulations, and as a result, significant disputes may arise with these tax authorities involving issues of the timing and amount of deductions and allocations of income among various tax jurisdictions. Resolution of one or more of these exposures in any reporting period could have a material impact on the results of operations for that period.

If we fail to attract and retain highly qualified personnel, we may be unable to successfully develop new product candidates, conduct our clinical trials and commercialize our product candidates.

Our future success will depend in large part on our continued ability to attract and retain highly qualified scientific, technical and management personnel, as well as personnel with expertise in clinical testing, governmental regulation and commercialization. We face competition for personnel from other companies, universities, public and private research institutions, government entities and other organizations. Competition for qualified personnel in the biopharmaceutical field is intense, and there is a limited pool of qualified potential employees to recruit. We may not be able to attract and retain quality personnel on acceptable terms. If we are unsuccessful in our recruitment and retention efforts, our business may be harmed.

There can be no assurance that we will pay dividends or continue to repurchase stock.

Our Board of Directors authorized a dividend program under which we intend to pay quarterly dividends of $0.47 per share, subject to quarterly declarations by our Board of Directors. Our Board of Directors also approved the repurchase of up to an additional $12.0 billion of our common stock. Any future declarations, amount and timing of any dividends and/or the amount and timing of such stock repurchases are subject to capital availability and determinations by our Board of Directors that cash dividends and/or stock repurchases are in the best interest of our stockholders and are in compliance with all respective laws and our agreements applicable to the declaration and payment of cash dividends and the repurchase of stock. Our ability to pay dividends and/or repurchase stock will depend upon, among other factors, our cash balances and potential future capital requirements for strategic

transactions, including acquisitions, debt service requirements, results of operations, financial condition and other factors beyond our control that our Board of Directors may deem relevant. A reduction in or elimination of our dividend payments, our dividend program and/or stock repurchases could have a negative effect on our stock price.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Issuer Purchases of Equity Securities

In April 2016, we completed the $15.0 billion share repurchase program authorized in January 2015 (2015 Program). In February 2016, our Board of Directors authorized a $12.0 billion share repurchase program (2016 Program) under which repurchases may be made in the open market or in privately negotiated transactions.

During the second quarter of 2016, we repurchased approximately 10 million shares of our common stock for an aggregate purchase price of $1.0 billion through open market transactions.

The table below summarizes our stock repurchase activity under both 2015 and 2016 Programs for the three months ended June 30, 2016:

| | Total Number of Shares Purchased (in thousands) | Average Price Paid per Share (in dollars) | Total Number of Shares Purchased as Part of Publicly Announced Program (in thousands) | Maximum Fair Value of Shares that May Yet Be Purchased Under the Program (in millions) |
|---|---|---|---|---|
| 2015 Program | | | | |
| April 1 - April 30, 2016 | 8,149 [2] | $ 92.09 [2] | 8,149 [2] | $ — |
| 2016 Program | | | | |
| April 1 - April 30, 2016 | 8,490 | $ 97.82 | 8,466 | $ 11,172 |
| May 1 - May 31, 2016 | 1,214 | $ 85.52 | 1,178 | $ 11,071 |
| June 1 - June 30, 2016 | 867 | $ 84.22 | 844 | $ 11,000 |
| Total | 18,720 [1] | $ 93.90 | 18,637 [1] | |

(1) The difference between the total number of shares purchased and the total number of shares purchased as part of publicly announced programs is due to shares of common stock withheld by us from employee restricted stock awards in order to satisfy applicable tax withholding obligations.

(2) In February 2016, we entered into an accelerated stock repurchase program (ASR) to purchase $5.0 billion of our common stock under our 2015 Program. We made an upfront payment of $5.0 billion and received 46 million shares of our common stock under the ASR program. In April 2016, at the end of the purchase period, the ASR was settled and an additional 8 million shares were received and retired. In total, 54 million shares were received under this ASR at an average repurchase price of $92.09 per share.

Item 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

Item 5. OTHER INFORMATION

Not applicable.

Item 6. EXHIBITS

Reference is made to the Exhibit Index included herein.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

GILEAD SCIENCES, INC.
(Registrant)

Date: August 5, 2016 /s/ JOHN F. MILLIGAN
John F. Milligan, Ph.D.
President and Chief Executive Officer
(Principal Executive Officer)

Date: August 5, 2016 /s/ ROBIN L. WASHINGTON
Robin L. Washington
Executive Vice President and Chief Financial Officer
(Principal Financial and Accounting Officer)

Exhibit Index

| Exhibit Footnote | Exhibit Number | Description of Document |
|---|---|---|
| (1) | 1.1 | Underwriting Agreement, dated September 9, 2015, among Registrant and Merrill Lynch, Pierce, Fenner & Smith Incorporated and J.P. Morgan Securities LLC, as representatives of the several underwriters listed in Schedule 1 thereto |
| †(2) | 2.1 | Agreement and Plan of Merger among Registrant, Merger Sub and Pharmasset, Inc., dated as of November 21, 2011 |
| (3) | 3.1 | Restated Certificate of Incorporation of Registrant |
| (4) | 3.2 | Amended and Restated Bylaws of Registrant |
| | 4.1 | Reference is made to Exhibit 3.1 and Exhibit 3.2 |
| (5) | 4.2 | Indenture related to Senior Notes, dated as of March 30, 2011, between Registrant and Wells Fargo, National Association, as Trustee |
| (5) | 4.3 | First Supplemental Indenture related to Senior Notes, dated as of March 30, 2011, between Registrant and Wells Fargo, National Association, as Trustee (including form of Senior Notes) |
| (6) | 4.4 | Second Supplemental Indenture related to Senior Notes, dated as of December 13, 2011, between Registrant and Wells Fargo, National Association, as Trustee (including Form of 2014 Note, Form of 2016 Note, Form of 2021 Note, Form of 2041 Note) |
| (7) | 4.5 | Third Supplemental Indenture related to Senior Notes, dated as of March 7, 2014, between Registrant and Wells Fargo, National Association, as Trustee (including Form of 2019 Note, Form of 2024 Note, Form of 2044 Note) |
| (8) | 4.6 | Fourth Supplemental Indenture related to Senior Notes, dated as of November 17, 2014, between Registrant and Wells Fargo, National Association, as Trustee (including Form of 2020 Note, Form of 2025 Note, Form of 2045 Note) |
| (1) | 4.7 | Fifth Supplemental Indenture, dated as of September 14, 2015, between Registrant and Wells Fargo Bank, National Association, as Trustee (including Form of 2018 Note, Form of 2020 Note, Form of 2022 Note, Form of 2026 Note, Form of 2035 Note and Form of 2046 Note) |
| (9) | 10.1 | Confirmation of OTC Warrant Transaction, dated July 26, 2010, between Registrant and Goldman, Sachs & Co. for warrants expiring in 2016 |
| (9) | 10.2 | Confirmation of OTC Warrant Transaction, dated July 26, 2010, between Registrant and JPMorgan Chase Bank, National Association for warrants expiring in 2016 |
| (10) | 10.3 | Confirmation of OTC Additional Warrant Transaction, dated August 5, 2010, between Registrant and Goldman, Sachs & Co. for warrants expiring in 2016 |
| (10) | 10.4 | Confirmation of OTC Additional Warrant Transaction, dated August 5, 2010, between Registrant and JPMorgan Chase Bank, National Association for warrants expiring in 2016 |

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| (11) | 10.5 | Amendment to Base Warrants (2016), dated May 8, 2015, between Registrant and Goldman, Sachs & Co. |
| (11) | 10.6 | Amendment to Base Warrants (2016), dated May 8, 2015, between Registrant and JPMorgan Chase Bank, National Association |
| *(3) | 10.7 | Gilead Sciences, Inc. 2004 Equity Incentive Plan, as amended through May 8, 2013 |
| *(12) | 10.8 | Form of employee stock option agreement used under 2004 Equity Incentive Plan (for grants prior to February 2008) |
| *(13) | 10.9 | Form of employee stock option agreement used under 2004 Equity Incentive Plan (for grants made February 2008 through April 2009) |
| *(14) | 10.10 | Form of employee stock option agreement used under 2004 Equity Incentive Plan (for grants commencing in May 2009) |
| *(15) | 10.11 | Form of employee stock option agreement used under 2004 Equity Incentive Plan (for grants commencing in February 2010) |
| *(16) | 10.12 | Form of employee stock option agreement used under 2004 Equity Incentive Plan (for 2011 and subsequent year grants) |
| *(13) | 10.13 | Form of non-employee director stock option agreement used under 2004 Equity Incentive Plan (for grants prior to 2008) |
| *(13) | 10.14 | Form of non-employee director option agreement used under 2004 Equity Incentive Plan (for initial grants made in 2008) |
| *(13) | 10.15 | Form of non-employee director option agreement used under 2004 Equity Incentive Plan (for annual grants made in May 2008 and through May 2012) |
| *(14) | 10.16 | Form of non-employee director option agreement used under 2004 Equity Incentive Plan (for annual grants commencing in May 2009 and through May 2012) |
| *(17) | 10.17 | Form of non-employee director option agreement used under 2004 Equity Incentive Plan (for annual grants made in May 2013) |
| *(17) | 10.18 | Form of non-employee director option agreement (non-U.S.) used under 2004 Equity Incentive Plan (for annual grants made in May 2013) |
| *(18) | 10.19 | Form of non-employee director option agreement used under 2004 Equity Incentive Plan (for annual grants made in and after May 2014) |
| *(19) | 10.20 | Form of restricted stock unit issuance agreement used under 2004 Equity Incentive Plan (for annual grants to non-employee directors in May 2012) |
| *(14) | 10.21 | Form of restricted stock award agreement used under 2004 Equity Incentive Plan (for annual grants to certain non-employee directors prior to May 2012) |
| *(17) | 10.22 | |

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| | | Form of restricted stock unit issuance agreement used under 2004 Equity Incentive Plan (for annual grants to non-employee directors commencing in May 2013) |
| *(18) | 10.23 | Form of restricted stock unit issuance agreement used under 2004 Equity Incentive Plan (for annual grants to non-employee directors commencing in and after May 2014) |
| *(17) | 10.24 | Form of restricted stock unit issuance agreement (non-U.S.) used under 2004 Equity Incentive Plan (for annual grants to non-employee directors commencing in May 2013) |
| *(14) | 10.25 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for grants to certain executive officers made in 2009) |
| *(15) | 10.26 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for grants to certain executive officers made in 2010) |
| *(16) | 10.27 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for grants to certain executive officers made in 2011) |
| *(17) | 10.28 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for grants to certain executive officers made in 2012) |
| *(20) | 10.29 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for TSR Goals in 2013 and 2014) |
| *(21) | 10.30 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for TSR Goals (US) in 2016) |
| *(21) | 10.31 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for TSR Goals (US) with Director Retirement Provisions in 2016 ) |
| *(22) | 10.32 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for Revenue Goals in 2013 and 2014) |
| *(21) | 10.33 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for Revenue Goals (US) in 2016) |
| *(21) | 10.34 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for Revenue Goals (US) with Director Retirement Provisions in 2016) |
| *(23) | 10.35 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for TSR Goals - Non-US in 2015) |
| *(21) | 10.36 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for TSR Goals -Non-US in 2016) |
| *(23) | 10.37 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for Revenue Goals - Non-US in 2015) |
| *(21) | 10.38 | Form of performance share award agreement used under the 2004 Equity Incentive Plan (for Revenue Goals - Non-US in 2016) |

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| *(24) | 10.39 | Form of restricted stock unit issuance agreement used under the 2004 Equity Incentive Plan (for grants to certain executive officers made prior to May 2009) |
| *(14) | 10.40 | Form of restricted stock unit issuance agreement used under the 2004 Equity Incentive Plan (for grants to certain executive officers commencing in May 2009) |
| *(25) | 10.41 | Form of restricted stock unit issuance agreement used under the 2004 Equity Incentive Plan (service-based vesting for certain executive officers commencing in November 2009) |
| *(16) | 10.42 | Form of restricted stock unit issuance agreement used under the 2004 Equity Incentive Plan (service-based vesting for certain executive officers commencing in 2011) |
| *(26) | 10.43 | Gilead Sciences, Inc. Employee Stock Purchase Plan, restated on January 22, 2015 |
| *(27) | 10.44 | Gilead Sciences, Inc. Deferred Compensation Plan-Basic Plan Document |
| *(25) | 10.45 | Gilead Sciences, Inc. Deferred Compensation Plan-Adoption Agreement |
| *(27) | 10.46 | Addendum to the Gilead Sciences, Inc. Deferred Compensation Plan |
| *(28) | 10.47 | Gilead Sciences, Inc. 2005 Deferred Compensation Plan, as amended and restated on October 23, 2008 |
| *(29) | 10.48 | Gilead Sciences, Inc. Severance Plan, as amended on March 8, 2016 |
| *(30) | 10.49 | Gilead Sciences, Inc. Corporate Bonus Plan, amended on November 4, 2015 |
| *(31) | 10.50 | Amended and Restated Gilead Sciences, Inc. Code Section 162(m) Bonus Plan |
| *(32) | 10.51 | 2016 Base Salaries for the Named Executive Officers |
| *(33) | 10.52 | Offer Letter dated April 16, 2008 between Registrant and Robin Washington |
| * | 10.53 | Offer Letter dated May 20, 2016 between Registrant and Kevin Young |
| *(34) | 10.54 | Form of Indemnity Agreement entered into between Registrant and its directors and executive officers |
| *(35) | 10.55 | Form of Employee Proprietary Information and Invention Agreement entered into between Registrant and certain of its officers and key employees |
| *(15) | 10.56 | Form of Employee Proprietary Information and Invention Agreement entered into between Registrant and certain of its officers and key employees (revised in September 2006) |
| +(36) | 10.57 | Amended and Restated Collaboration Agreement by and among Registrant, Gilead Holdings, LLC, Bristol-Myers Squibb Company, E.R. Squibb & Sons, L.L.C., and Bristol-Myers Squibb & Gilead Sciences, LLC, dated September 28, 2006 |
| +(13) | 10.58 | Commercialization Agreement by and between Gilead Sciences Ireland UC (formerly Gilead Sciences Limited) and Bristol-Myers Squibb Company, dated December 10, 2007 |

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| + (37) | 10.59 | Amendment Agreement, dated October 25, 1993, between Registrant, the Institute of Organic Chemistry and Biochemistry (IOCB) and Rega Stichting v.z.w. (REGA), together with the following exhibits: the License Agreement, dated December 15, 1991, between Registrant, IOCB and REGA (the 1991 License Agreement), the License Agreement, dated October 15, 1992, between Registrant, IOCB and REGA (the October 1992 License Agreement) and the License Agreement, dated December 1, 1992, between Registrant, IOCB and REGA (the December 1992 License Agreement) |
| + (38) | 10.60 | Amendment Agreement between Registrant and IOCB/REGA, dated December 27, 2000 amending the 1991 License Agreement and the December 1992 License Agreement |
| + (36) | 10.61 | Sixth Amendment Agreement to the License Agreement, between IOCB/REGA and Registrant, dated August 18, 2006 amending the October 1992 License Agreement and the December 1992 License Agreement |
| + (39) | 10.62 | Seventh Amendment Agreement to the License Agreement, between IOCB/REGA and Registrant dated July 1, 2013 amending the October 1992 License Agreement and the December 1992 License Agreement |
| + (40) | 10.63 | Exclusive License Agreement between Registrant (as successor to Triangle Pharmaceuticals, Inc.), Glaxo Group Limited, The Wellcome Foundation Limited, Glaxo Wellcome Inc. and Emory University, dated May 6, 1999 |
| + (41) | 10.64 | Royalty Sale Agreement by and among Registrant, Emory University and Investors Trust & Custodial Services (Ireland) Limited, solely in its capacity as Trustee of Royalty Pharma, dated July 18, 2005 |
| + (41) | 10.65 | Amended and Restated License Agreement between Registrant, Emory University and Investors Trust & Custodial Services (Ireland) Limited, solely in its capacity as Trustee of Royalty Pharma, dated July 21, 2005 |
| + (42) | 10.66 | License Agreement between Japan Tobacco Inc. and Registrant, dated March 22, 2005 |
| + (43) | 10.67 | First Amendment to License Agreement between Japan Tobacco Inc. and Registrant, dated May 19, 2005 |
| + (43) | 10.68 | Second Amendment to License Agreement between Japan Tobacco Inc. and Registrant, dated May 17, 2010 |
| +(11) | 10.69 | Third Amendment (Revised) to License Agreement between Japan Tobacco Inc. and Registrant, dated June 10, 2015 |
| + (43) | 10.70 | Fourth Amendment to License Agreement between Japan Tobacco Inc. and Registrant, dated July 5, 2011 |
| +(44) | 10.71 | Amendment to License Agreement between Japan Tobacco Inc. and Registrant, dated October 10, 2013 |
| +(45) | 10.72 | Fifth Amendment to License Agreement between Japan Tobacco Inc. and Registrant, dated September 29, 2014 |

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| +(46) | 10.73 | Amended and Restated Collaboration Agreement by and among Registrant, Gilead Sciences Ireland UC (formerly Gilead Sciences Limited) and Janssen R&D Ireland, dated December 23, 2014 |
| +(47) | 10.74 | Master Clinical and Commercial Supply Agreement between Gilead World Markets, Limited, Registrant and Patheon Inc., dated January 1, 2003 |
| +(48) | 10.75 | Restated and Amended Toll Manufacturing Agreement between Gilead Sciences Ireland UC (formerly Gilead Sciences Limited), Registrant and Takeda GmbH (formerly Nycomed GmbH and Altana Pharma Oranienburg GmbH), dated November 7, 2005 |
| | 31.1 | Certification of Chief Executive Officer, as required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended |
| | 31.2 | Certification of Chief Financial Officer, as required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended |
| | 32.1** | Certifications of Chief Executive Officer and Chief Financial Officer, as required by Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. §1350) |
| | 101*** | The following materials from Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2016, formatted in Extensible Business Reporting Language (XBRL) includes: (i) Condensed Consolidated Balance Sheets, (ii) Condensed Consolidated Statements of Income, (iii) Condensed Consolidated Statements of Comprehensive Income, (iv) Condensed Consolidated Statements of Cash Flows and (v) Notes to Condensed Consolidated Financial Statements. |

(1) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on September 14, 2015, and incorporated herein by reference.
(2) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on November 25, 2011, and incorporated herein by reference.
(3) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on May 8, 2014, and incorporated herein by reference.
(4) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on December 23, 2015, and incorporated herein by reference.
(5) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on April 1, 2011, and incorporated herein by reference.
(6) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on December 13, 2011, and incorporated herein by reference.
(7) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on March 7, 2014, and incorporated herein by reference.
(8) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on November 17, 2014, and incorporated herein by reference.
(9) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2010, and incorporated herein by reference.
(10) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2010, and incorporated herein by reference.
(11) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2015, and incorporated herein by reference.

(12) Filed as an exhibit to Registrant's Current Report on Form 8-K/A filed on February 22, 2006, and incorporated herein by reference.
(13) Filed as an exhibit to Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2007, and incorporated herein by reference.
(14) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2009, and incorporated herein by reference.
(15) Filed as an exhibit to Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2009, and incorporated herein by reference.
(16) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2011, and incorporated herein by reference.
(17) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2013, and incorporated herein by reference
(18) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2014, and incorporated herein by reference.
(19) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, and incorporated herein by reference.
(20) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2012, and incorporated herein by reference.
(21) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2016, and incorporated herein by reference.
(22) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2013, and incorporated herein by reference.
(23) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2015, and incorporated herein by reference.
(24) Filed as an exhibit to Registrant's Current Report on Form 8-K first filed on December 19, 2007, and incorporated herein by reference.
(25) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2010, and incorporated herein by reference.
(26) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on May 8, 2015, and incorporated herein by reference.
(27) Filed as an exhibit to Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2001, and incorporated herein by reference.
(28) Filed as an exhibit to Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2008, and incorporated herein by reference.
(29) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on March 8, 2016, and incorporated herein by reference.
(30) Filed as an exhibit to Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2015, and incorporated herein by reference.
(31) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on May 17, 2016, and incorporated herein by reference.
(32) Filed as an exhibit to Registrant's Current Report on Form 8-K filed on February 3, 2016, and incorporated herein by reference.
(33) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2008, and incorporated herein by reference.
(34) Filed as an exhibit to Registrant's Registration Statement on Form S-1 (No. 33-55680), as amended, and incorporated herein by reference.
(35) Filed as an exhibit to Registrant's Registration Statement on Form S-8 (No. 333-102912) filed on January 31, 2003, and incorporated herein by reference.
(36) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2006, and incorporated herein by reference.

(37) Filed as an exhibit to Registrant's Annual Report on Form 10-K for the fiscal year ended March 31, 1994, and incorporated herein by reference.
(38) Filed as an exhibit to Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2000, and incorporated herein by reference.
(39) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2013, and incorporated herein by reference.
(40) Filed as an exhibit to Triangle Pharmaceuticals, Inc.'s Quarterly Report on Form 10-Q/A filed on November 3, 1999, and incorporated herein by reference.
(41) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2005, and incorporated herein by reference.
(42) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005, and incorporated herein by reference.
(43) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2011, and incorporated herein by reference.
(44) Filed as an exhibit to Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2013, and incorporated herein by reference.
(45) Filed as an exhibit to Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2014, and incorporated herein by reference.
(46) Filed as an exhibit to Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2014, and incorporated herein by reference.
(47) Filed as an exhibit to Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2003, and incorporated herein by reference.
(48) Filed as an exhibit to Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2005, and incorporated herein by reference.

† The Agreement and Plan of Merger (the Pharmasset Merger Agreement) contains representations and warranties of Registrant, Merger Sub and Pharmasset, Inc. made solely to each other as of specific dates. Those representations and warranties were made solely for purposes of the Pharmasset Merger Agreement and may be subject to important qualifications and limitations agreed to by Registrant, Merger Sub and Pharmasset, Inc. Moreover, some of those representations and warranties may not be accurate or complete as of any specified date, may be subject to a standard of materiality provided for in the Pharmasset Merger Agreement and have been used for the purpose of allocating risk among Registrant, Merger Sub and Pharmasset, Inc. rather than establishing matters as facts.

* Management contract or compensatory plan or arrangement.

** This certification accompanies the Form 10-K to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of Registrant under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before or after the date of the Form 10-K), irrespective of any general incorporation language contained in such filing.

*** XBRL information is filed herewith.

+ Certain confidential portions of this Exhibit were omitted by means of marking such portions with an asterisk (the Mark). This Exhibit has been filed separately with the Secretary of the Securities and Exchange Commission without the Mark pursuant to Registrant's Application Requesting Confidential Treatment under Rule 24b-2 under the Securities Exchange Act of 1934, as amended.