

SERONO S A
Form 6-K
October 19, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 6-K

**REPORT OF FOREIGN PRIVATE ISSUER PURSUANT TO RULE 13a-16 OR
15d-16 UNDER THE SECURITIES EXCHANGE ACT OF 1934**

For the month of October

Commission File Number 1-15096

Serono S.A.

(Translation of registrant's name into English)

**15 bis, Chemin des Mines
Case Postale 54
CH-1211 Geneva 20
Switzerland**

(Address of principal executive office)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F. Form 20-F Form 40-F

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1):

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7):

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934. Yes No

If Yes is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-_____.

Media Release

FOR IMMEDIATE RELEASE

Serono Delivers Strong Adjusted* Net Income of \$183.5m in Third Quarter 2006

- Excellent performance of Rebif® with sales up 18.7% to \$374.8m -

Geneva, Switzerland, October 19, 2006 Serono (virt-x: SEO and NYSE: SRA) today reported its third quarter results for the period ended September 30, 2006.

Key Points for Third Quarter 2006

- Total revenues of \$699.1m, up 9.5%
- Product sales up 8.4% to \$619.2m
- Rebif® sales up 18.7% to \$374.8m worldwide and up 30.1% to \$133.3m in USA
- Operating margin of 28.6% of total revenues, up from 25.0% in Q3 2005
- Reported net income of \$170.6m, up 19.8%
- Reported basic EPS of \$11.64 per bearer share and \$0.29 per ADS
- Continued good progress in several R&D programs:
 - In-licensing of safinamide in early Phase 3 in Parkinson's Disease
 - Fast Track designation for oral cladribine in relapsing forms of multiple sclerosis
 - Rebif New Formulation (RNF) 12-month results presented substantially improved tolerability and much lower immunogenicity compared with historical data **
 - Aurora kinase inhibitor oncology project moved to Phase 1

We have delivered an excellent quarter with strong performance of our leading product, Rebif®, and our company has again generated strong cash flow, said Ernesto Bertarelli, Chief Executive Officer. Our investment in R&D has yielded good progress in several clinical programs.

During the third quarter of 2006, we sustained the operating leverage we established over the last 18 months resulting in higher operating margin and strong growth on the bottom line, said Stuart Grant, Chief Financial Officer.

* Non-IFRS earnings measure which excludes a \$13.0m charge related to the revised carrying value of the convertible bond in Q3 2006.

** The new formulation of Rebif® is currently under regulatory review by the European Medicines Agency, the US Food and Drug Administration and other healthcare authorities.

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Financial Performance

Total revenues increased by 9.5%, or 7.0% in local currencies, to \$699.1m in the third quarter of 2006 (Q3 2005: \$638.3m). Product sales grew 8.4%, or 5.7% in local currencies, to \$619.2m (Q3 2005: \$571.5m). Royalty and license income increased by 19.4% to \$79.8m (Q3 2005: \$66.9m), representing 11.4% of revenues.

Gross margin continues to be strong at 88.6% of product sales (Q3 2005: 88.6%). Selling, General and Administrative expenses were \$226.1m (Q3 2005: \$201.3m) while Research and Development expenses were \$141.3m (Q3 2005: \$146.9m). Other operating expenses were down 6.4% to \$61.7m (Q3 2005: \$65.9m).

Operating income in the third quarter of 2006 was up 25.2% to \$199.6m (Q3 2005: \$159.4m). Continued operational leverage has delivered an operating margin of 28.6% of total revenues compared to 25.0% of total revenues in the same period last year.

Financial income was \$23.2m (Q3 2005: \$17.3m) and financial expense was \$19.7m (Q3 2005: \$5.9m) including a \$13.0m charge related to the revised carrying value of the convertible bond as a consequence of the anticipated change of control.

Reported net income in the third quarter of 2006 was \$170.6m up 19.8% (Q3 2005: \$142.4m), leading to a net margin of 24.4% of total revenues (Q3 2005: 22.3% of total revenues). Basic earnings per share in the third quarter of 2006 were up 19.1% to \$11.64 per bearer share (Q3 2005: \$9.77) and \$0.29 per American Depositary Share (Q3 2005: \$0.24).

On an adjusted basis, net income increased 15.5% to \$183.5m from \$158.9m in the prior year. Adjustments included an \$18.3m charge related to the transfer of the Serono Genetics Institute in the third quarter 2005 and a \$13.0m charge related to the convertible bond taken in the third quarter 2006.

For the first nine months, net cash flow from operating activities before change in working capital was \$750.0m (YTD 2005: \$555.0m), or \$622.7m after change in working capital (YTD 2005: \$439.5m). The company's liquid financial assets were \$2.1 billion at the end of the third quarter 2006.

As of September 30, 2006, there were 14,661,190 outstanding equivalent bearer shares of Serono S.A., net of treasury shares. The total weighted average number of equivalent bearer shares of Serono S.A. was 14,654,546 for the three months ending September 30, 2006.

Key Product Sales

In the third quarter of 2006, Rebif® had an excellent performance with worldwide sales of \$374.8m, up 18.7%, or 15.4% in local currencies (Q3 2005: \$315.6m). Rebif® continues to be the best-selling therapy for multiple sclerosis outside the US, with sales of \$241.5m, growing 13.3%, or 8.2% in local currencies (Q3 2005: \$213.2m). More than four years after launch in the US, Rebif®

continues to grow strongly and reached US sales of \$133.3m, up 30.1% (Q3 2005: \$102.5m).

Novantrone® sales in the third quarter of 2006 were \$2.8m, down 84.6%, consequent to the introduction of generics of mitoxantrone in the US in April 2006 (Q3 2005: \$18.2m).

Sales of Gonal-f® were \$122.8m in line with the third quarter of 2005 (Q3 2005: \$125.6m). Global sales of supporting products (Ovidrel®, Cetrotide®, Crinone® and Luveris®) were up 11.5%, or 9.5% in local currencies to \$21.9m (Q3 2005: \$19.6m).

Saizen® sales were \$50.5m (Q3 2005: \$50.8m), while Serostim® sales grew 9.5% to \$19.5m (Q3 2005: \$17.8m).

Sales of Raptiva® were up 80.6% to \$18.1m in the third quarter 2006 (Q3 2005: \$10.0m).

R&D News

Serono has reported notable progress in its Neurology R&D pipeline during the last three months:

- Serono has recently announced an agreement with Newron Pharmaceuticals SpA under which Serono is granted exclusive worldwide rights for the development of safinamide in Parkinson's disease, Alzheimer's disease, and other cognitive disorders. Positive results from a Phase 3 study of safinamide in Parkinson's disease were reported in June 2006.
- In September 2006, oral cladribine was designated a Fast Track product for patients with relapsing forms of multiple sclerosis by the US Food and Drug Administration. Under Fast Track designation oral cladribine is eligible for Priority Review. Patient enrollment into the ongoing Phase 3 pivotal trial is planned to be completed by the end of 2006.
- Data on a new formulation of Rebif® demonstrating a substantial improvement in tolerability and reduction in antibody formation at one year, compared with historical data from patients, were recently presented at the 22nd ECTRIMS congress.

In the third quarter of 2006, Serono further advanced its R&D initiatives in oncology:

- Serono began enrolling patients in a Phase 1 study evaluating the safety and tolerability of R763, a highly potent, orally available multi-Aurora kinase inhibitor, for the treatment of patients with refractory solid tumors in September 2006.
 - With respect to adecatumumab, final data from two Phase 2 clinical trials showed activity in both metastatic breast cancer and prostate cancer. While neither study reached its primary endpoint, good tolerability and encouraging trends towards higher activity for patients with high levels of EpCAM overexpression and treated at higher doses were observed. Serono and Micromet continue to investigate opportunities for further development.
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In September 2006, Serono and Syntonix Pharmaceuticals Inc. entered into an agreement to pursue the development of a long-acting FSH therapy for the treatment of infertility that can be inhaled and dosed less frequently, instead of injected daily.

Conference Call and Webcast

Serono will hold a conference call on October 19, 2006, starting at 3.00 pm Central European Time (9.00 am U.S. Eastern Time) during which Serono Management will present the Company's Third Quarter 2006 results. To join the telephone conference please dial 1 866 291 4166 (from the US), 091 610 5600 (from Switzerland), 0207 107 0611 (from the UK) and +41 91 610 5600 (from elsewhere). The event will also be relayed by live audio webcast, which interested parties may access via Serono's Corporate home page, www.serono.com. A link to the webcast will be provided immediately prior to the event and will be available for replay following the event. Additionally, the webcast will be available for replay until close of business on November 24, 2006.

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Forward-looking statements

Some of the statements in this press release are forward looking. Such statements are inherently subject to known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements of Serono S.A. and affiliates to be materially different from those expected or anticipated in the forward-looking statements. Forward-looking statements are based on Serono's current expectations and assumptions, which may be affected by a number of factors, including those discussed in this press release and more fully described in Serono's Annual Report on Form 20-F filed with the U.S. Securities and Exchange Commission on February 28, 2006. These factors include any failure or delay in Serono's ability to develop new products, any failure to receive anticipated regulatory approvals, any problems in commercializing current products as a result of competition or other factors, our ability to obtain reimbursement coverage for our products, the outcome of any government investigations and litigation. Serono is providing this information as of the date of this press release, and has no responsibility to update the forward-looking statements contained in this press release to reflect events or circumstances occurring after the date of this press release.

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About Serono

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Serono is a global biotechnology leader. The Company has eight biotechnology products, Rebif®, Gonal-f®, Luveris®, Ovidrel®/Ovitrelle®, Serostim®, Saizen®, Zorbtive and Raptiva®. In addition to being the world leader in reproductive health, Serono has strong market positions in neurology, metabolism and growth and has recently entered the psoriasis area. The Company's research programs are focused on growing these businesses and on establishing new therapeutic areas, including oncology and autoimmune diseases.

In 2005, Serono, whose products are sold in over 90 countries, achieved worldwide revenues of US\$2,586.4 million. Reported net loss in 2005 was US\$106.1 million, reflecting a charge of US\$725 million taken relating to the settlement of the US Attorney's Office investigation of Serostim. Excluding this charge as well as other non-recurring items, adjusted net income grew 28.4% to US\$565.3 million in 2005. Bearer shares of Serono S.A., the holding company, are traded on the virt-x (SEO) and its American Depositary Shares are traded on the New York Stock Exchange (SRA).

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On the following pages, there are:

- Tables detailing sales in dollars by therapeutic area, geographic region and the top 10 products for the 3 and 9 months ended September 30, 2006 and 2005.
 - Consolidated income statements for the 3 and 9 months ended September 30, 2006 and 2005; adjusted net income and adjusted earnings per share for the 3 and 9 months ended September 30, 2006 and 2005; the consolidated balance sheets as of September 30, 2006 and December 31, 2005; the consolidated statements of changes in equity as of September 30, 2006 and 2005; the consolidated statements of cash flows for the 9 months ended September 30, 2006 and 2005; the selected explanatory notes to the consolidated financial statements. These consolidated financial statements have been prepared on the basis of International Financial Reporting Standards.
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Sales by therapeutic area

| | Three Months Ended September 30, 2006 | | | Three Months Ended September 30, 2005 | | |
|-----------------------------------|--|------------|--------------|--|------------|----------|
| | \$ million | % of sales | % change \$ | \$ million | % of sales | |
| Neurology | 375.7 | 60.7 | % 16.7 | % 321.9 | 56.3 | % |
| Reproductive Health | 150.6 | 24.3 | % (1.4) |)% 152.8 | 26.7 | % |
| Growth & Metabolism | 70.2 | 11.3 | % 1.8 | % 69.0 | 12.1 | % |
| Dermatology | 18.1 | 2.9 | % 80.6 | % 10.0 | 1.8 | % |
| Others | 4.5 | 0.8 | % (74.6) |)% 17.8 | 3.1 | % |
| Total sales (US\$ million) | \$ 619.2 | 100 | % 8.4 | % \$ 571.5 | 100 | % |

Sales by geographic region

| | Three Months Ended September 30, 2006 | | | Three Months Ended September 30, 2005 | | |
|-----------------------------------|--|------------|--------------|--|------------|----------|
| | \$ million | % of sales | % change \$ | \$ million | % of sales | |
| Western Europe | 265.9 | 42.9 | % 10.4 | % 241.0 | 42.2 | % |
| North America | 232.1 | 37.5 | % 7.5 | % 215.9 | 37.8 | % |
| Latin America | 35.3 | 5.7 | % 13.1 | % 31.2 | 5.5 | % |
| Others | 85.8 | 13.9 | % 3.0 | % 83.3 | 14.5 | % |
| Total sales (US\$ million) | \$ 619.2 | 100 | % 8.4 | % \$ 571.5 | 100 | % |

Sales by therapeutic area

| | Nine Months Ended September 30, 2006 | | | Nine Months Ended September 30, 2005 | | |
|-----------------------------------|---|------------|--------------|---|------------|----------|
| | \$ million | % of sales | % change \$ | \$ million | % of sales | |
| Neurology | 1 071.9 | 58.2 | % 12.6 | % 951.5 | 54.9 | % |
| Reproductive Health | 488.1 | 26.5 | % (2.0) |)% 498.1 | 28.7 | % |
| Growth & Metabolism | 207.6 | 11.3 | % 0.5 | % 206.5 | 11.9 | % |
| Dermatology | 48.7 | 2.6 | % 123.0 | % 21.8 | 1.3 | % |
| Others | 26.5 | 1.4 | % (53.1) |)% 56.4 | 3.2 | % |
| Total sales (US\$ million) | \$ 1 842.7 | 100 | % 6.2 | % \$ 1 734.4 | 100 | % |

Sales by geographic region

| | Nine Months Ended September 30, 2006 | | | Nine Months Ended September 30, 2005 | | |
|-----------------------------------|---|------------|--------------|---|------------|----------|
| | \$ million | % of sales | % change \$ | \$ million | % of sales | |
| Western Europe | 820.8 | 44.5 | % 4.8 | % 783.5 | 45.2 | % |
| North America | 667.0 | 36.2 | % 8.0 | % 617.4 | 35.6 | % |
| Latin America | 101.1 | 5.5 | % 8.6 | % 93.1 | 5.4 | % |
| Others | 253.8 | 13.8 | % 5.6 | % 240.4 | 13.8 | % |
| Total sales (US\$ million) | \$ 1 842.7 | 100 | % 6.2 | % \$ 1 734.4 | 100 | % |

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TOP TEN PRODUCTS

| * TA | | Three Months Ended September 30, 2006 | | | Three Months Ended September 30, 2005 | | |
|--------------|-------------|--|------------|-------------|--|------------|---|
| | | \$ million | % of sales | % change \$ | \$ million | % of sales | % |
| Rebif® | MS | 374.8 | 60.5 | % 18.7 | % 315.6 | 55.2 | % |
| Gonal-f® | RH | 122.8 | 19.8 | % (2.2) |)% 125.6 | 22.0 | % |
| Saizen® | Growth | 50.5 | 8.2 | % (0.7) |)% 50.8 | 8.9 | % |
| Serostim® | Wasting | 19.5 | 3.2 | % 9.5 | % 17.8 | 3.1 | % |
| Raptiva® | Dermatology | 18.1 | 2.9 | % 80.6 | % 10.0 | 1.8 | % |
| Ovidrel® | RH | 6.7 | 1.1 | % 26.9 | % 5.3 | 0.9 | % |
| Crinone® | RH | 6.6 | 1.1 | % 16.6 | % 5.6 | 1.0 | % |
| Cetrotide® | RH | 6.1 | 1.0 | % (3.2) |)% 6.3 | 1.1 | % |
| Novantrone® | MS/Oncology | 2.8 | 0.5 | % (84.6) |)% 18.2 | 3.2 | % |
| Metrodin-HP® | RH | 2.6 | 0.4 | % (24.9) |)% 3.5 | 0.6 | % |

| * TA | | Nine Months Ended September 30, 2006 | | | Nine Months Ended September 30, 2005 | | |
|--------------|-------------|---|------------|-------------|---|------------|---|
| | | \$ million | % of sales | % change \$ | \$ million | % of sales | % |
| Rebif® | MS | 1 063.3 | 57.7 | % 13.8 | % 934.4 | 53.9 | % |
| Gonal-f® | RH | 401.2 | 21.8 | % (3.0) |)% 413.5 | 23.8 | % |
| Saizen® | Growth | 154.2 | 8.4 | % 1.3 | % 152.2 | 8.8 | % |
| Serostim® | Wasting | 52.6 | 2.9 | % (1.4) |)% 53.4 | 3.1 | % |
| Raptiva® | Dermatology | 48.7 | 2.6 | % 123.0 | % 21.8 | 1.3 | % |
| Novantrone® | MS/Oncology | 25.6 | 1.4 | % (51.1) |)% 52.5 | 3.0 | % |
| Ovidrel® | RH | 20.6 | 1.1 | % 19.0 | % 17.3 | 1.0 | % |
| Cetrotide® | RH | 19.7 | 1.1 | % 5.2 | % 18.7 | 1.1 | % |
| Crinone® | RH | 19.5 | 1.1 | % 9.8 | % 17.7 | 1.0 | % |
| Metrodin-HP® | RH | 8.9 | 0.5 | % (17.6) |)% 10.8 | 0.6 | % |

* Therapeutic Areas

RH = Reproductive Health
MS = Multiple Sclerosis
Oncology = Oncology
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Wasting = AIDS Wasting
Growth = Growth Retardation
Dermatology = Dermatology

Third Quarter Consolidated Income Statements (unaudited)

| Three months September 30 | 2006 US\$ 000 | % of Revenues | % change | 2005 US\$ 000 | % of Revenues |
|--|-------------------|------------------|----------|------------------|------------------|
| Revenues | | | | | |
| Product sales | 619,205 | | 8.4 | % 571,472 | |
| Royalty and license income | 79,849 | | 19.4 | % 66,851 | |
| Total Revenues | 699,054 | 100.0 | % 9.5 | % 638,323 | 100.0 % |
| Operating Expenses | | | | | |
| Cost of product sales | (70,384) | | | (64,866) | |
| % of Sales | 11.4 | % | | 11.4 | % |
| Selling, general and administrative | (226,072) | 32.3 | % 12.3 | % (201,307) | 31.5 % |
| Research and development | (141,316) | 20.2 | % (3.8) | % (146,863) | 23.0 % |
| Other operating expense, net | (61,679) | 8.8 | % (6.4) | % (65,877) | 10.3 % |
| Total Operating Expenses | (499,451) | 71.4 | % 4.3 | % (478,913) | 75.0 % |
| Operating Income | 199,603 | 28.6 | % 25.2 | % 159,410 | 25.0 % |
| Financial income | 23,164 | | | 17,251 | |
| Financial expense | (19,727) | | | (5,861) | |
| Foreign currency (loss) / gain, net | (2,660) | | | 2,285 | |
| Share of (loss) / profit of associates | (32) | | | 26 | |
| Income Before Taxes | 200,348 | 28.7 | % 15.7 | % 173,111 | 27.1 % |
| Taxes | (29,736) | | | (30,724) | |
| Net Income | 170,612 | 24.4 | % 19.8 | % 142,387 | 22.3 % |
| Attributable to: | | | | | |
| Minority interest | 57 | | | 18 | |
| Equity holders of Serono S.A. | 170,555 | 24.4 | % 19.8 | % 142,369 | 22.3 % |

Three months September 30

% change

Basic Earnings per Share

| | | | | |
|------------------------------|-------|------|---|------|
| - Bearer shares | 11.64 | 19.1 | % | 9.77 |
| - Registered shares | 4.66 | 19.1 | % | 3.91 |
| - American depositary shares | 0.29 | 19.1 | % | 0.24 |

Diluted Earnings per Share

| | | | | |
|------------------------------|-------|------|---|------|
| - Bearer shares | 11.62 | 19.7 | % | 9.70 |
| - Registered shares | 4.65 | 19.7 | % | 3.88 |
| - American depositary shares | 0.29 | 19.7 | % | 0.24 |

Quarterly Basic Earnings per Share is calculated in accordance with IAS 33 - Earnings per Share by dividing the Net Income attributable to bearer equity holders of Serono S.A., \$170.6 million for the three months ended September 30, 2006 (September 30, 2005: \$142.4 million), by the weighted average number of shares outstanding during the period presented. This is 10,249,330 bearer shares (2005: 10,166,799) and 11,013,040 registered shares (2005: 11,013,040). The total weighted average number of bearer shares is 14,654,546 (September 30, 2005: 14,572,015) for the three months ended September 30, 2006. As each American depositary share represents ownership interest in one fortieth of bearer share, Basic and Diluted Earnings per American depositary share is calculated as one fortieth of the Basic and Diluted Earnings per bearer share.

For quarterly Diluted Earnings per Share, the weighted average number of bearer shares outstanding is adjusted to assume conversion of all potential dilutive shares arising from outstanding stock options and the convertible bond. The number of bearer shares used to calculate the Diluted Earnings per Share for the three months ended September 30, 2006 was 10,277,741 (September 30, 2005: 10,624,369). The effect of the convertible bond was excluded from the calculation of Diluted Earnings per Share for the three months ended September 30, 2006 as it was anti-dilutive.

The accompanying selected explanatory notes form an integral part of these financial statements.

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Consolidated Income Statements (unaudited)

| Nine months ended September 30 | 2006 US\$ 000 | % of Revenues | % change | 2005 US\$ 000 | % of Revenues |
|--|--------------------|------------------|----------|------------------|------------------|
| Revenues | | | | | |
| Product sales | 1,842,736 | | 6.2 | % 1,734,372 | |
| Royalty and license income | 222,960 | | 22.4 | % 182,088 | |
| Total Revenues | 2,065,696 | 100.0 | % 7.8 | % 1,916,460 | 100.0 % |
| Operating Expenses | | | | | |
| Cost of product sales | (213,015) | | | (198,861) | |
| % of Sales | 11.6 | % | | 11.5 | % |
| Selling, general and administrative | (671,308) | 32.5 | % 5.2 | % (638,422) | 33.3 % |
| Research and development | (394,593) | 19.1 | % (12.1) | %(448,922) | 23.4 % |
| Other operating expense, net | (184,195) | 8.9 | % (80.0) | %(920,612) | 48.0 % |
| Total Operating Expenses | (1,463,111) | 70.8 | % (33.7) | %(2,206,817) | 115.2 % |
| Operating Income / (Loss) | 602,585 | 29.2 | % 307.5 | % (290,357) | (15.2) % |
| Financial income | 65,587 | | | 73,042 | |
| Financial expense | (32,145) | | | (26,457) | |
| Foreign currency (loss) / gain, net | (6,149) | | | 4,531 | |
| Share of (loss) / profit of associates | (616) | | | 52 | |
| Income / (Loss) Before Taxes | 629,262 | 30.5 | % 363.1 | % (239,189) | (12.5) % |
| Taxes | (89,355) | | | (10,290) | |
| Net Income / (Loss) | 539,907 | 26.1 | % 316.4 | % (249,479) | (13.0) % |
| Attributable to: | | | | | |
| Minority interest | 176 | | | 778 | |
| Equity holders of Serono S.A. | 539,731 | 26.1 | % 315.7 | % (250,257) | (13.1) % |

| Nine months ended September 30 | 2006 US\$ | % change | 2005 US\$ |
|--|--------------|----------|--------------|
| Basic Earnings / (Loss) per Share | | | |
| - Bearer shares | 36.85 | 314.5 | % (17.18) |
| - Registered shares | 14.74 | 314.5 | % (6.87) |
| - American depositary shares | 0.92 | 314.5 | % (0.43) |
| Diluted Earnings / (Loss) per Share | | | |
| - Bearer shares | 36.77 | 314.0 | % (17.18) |
| - Registered shares | 14.71 | 314.0 | % (6.87) |
| - American depositary shares | 0.92 | 314.0 | % (0.43) |

Basic Earnings / (Loss) per Share is calculated in accordance with IAS 33 - Earnings per Share by dividing the Net Income / (Loss) attributable to bearer equity holders of Serono S.A., \$539.7 million for the nine months ended September 30, 2006 (September 30, 2005: net loss of \$250.3 million), by the weighted average number of shares outstanding during the period presented, being 10,241,279 bearer shares (2005: 10,160,991) and 11,013,040 registered shares (2005: 11,013,040). The total weighted average number of bearer shares is 14,646,495 (September 30, 2005: 14,566,207) for the nine months ended September 30, 2006. As each American depositary share represents ownership interest in one fortieth of bearer share, Basic and Diluted Earnings / (Loss) per American depositary share is calculated as one fortieth of the Basic and Diluted Earnings / (Loss) per bearer share.

For Diluted Earnings / (Loss) per Share, the weighted average number of bearer shares outstanding is adjusted to assume conversion of all potential dilutive shares arising from outstanding stock options and the convertible bond. The number of bearer shares used to calculate the Diluted Earnings per Share for the nine months ended September 30, 2006 was 10,274,378. The effect of the convertible bond was excluded from the calculation of Diluted Earnings / (Loss) per Share for the nine months ended September 30, 2006 and 2005 as they were anti-dilutive. The effect of outstanding stock options was excluded from the calculation of Diluted Loss per Share for the nine months ended September 30,

2005 as they were anti-dilutive.

The accompanying selected explanatory notes form an integral part of these financial statements.

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Adjusted net income and adjusted earnings per share

| Nine months ended September 30 | 2006 US\$ 000 | % of Revenues | % change | 2005 US\$ 000 | % of Revenues |
|---|------------------|------------------|----------|------------------|------------------|
| Net Income / (Loss) as reported | 539,907 | 26.1 | % 316.4 | % (249,479) | (13.0)% |
| Gain on sale of investment in Zymogenetics | (8,365) | | | | |
| Revised carrying value of convertible bond | 12,972 | | | | |
| Litigation expense and related costs | | | | 725,000 | |
| Tax impact on litigation expense and related costs | | | | (64,525) | |
| Provision for R&D site transfer | | | | 18,316 | |
| Tax impact on provision for R&D site transfer | | | | (1,758) | |
| Gain on sale of investment in Celgene | | | | (29,963) | |
| Tax impact on gain on sale of investment in Celgene | | | | 1,439 | |
| Impairment loss on investment in CancerVax | | | | 8,440 | |
| Adjusted Net Income | 544,514 | 26.4 | % 33.6 | % 407,470 | 21.3 % |
| Attributable to: | | | | | |
| Minority interest | 176 | | | 778 | |
| Equity holders of Serono S.A. | 544,338 | 26.4 | % 33.8 | % 406,692 | 21.2 % |

| Nine months ended September 30 | Adjusted basis 2006 US\$ | Adjusted basis % change | Adjusted basis 2005 US\$ |
|-----------------------------------|-----------------------------|----------------------------|-----------------------------|
| Basic Earnings per Share | | | |
| - Bearer shares | 37.17 | 33.1 | % 27.92 |
| - Registered shares | 14.87 | 33.1 | % 11.17 |
| - American depositary shares | 0.93 | 33.1 | % 0.70 |
| Diluted Earnings per Share | | | |
| - Bearer shares | 37.08 | 33.4 | % 27.81 |
| - Registered shares | 14.83 | 33.4 | % 11.12 |
| - American depositary shares | 0.93 | 33.4 | % 0.70 |

| Three months September 30 | 2006 US\$ 000 | % of Revenues | % change | 2005 US\$ 000 | % of Revenues |
|---|------------------|------------------|----------|------------------|------------------|
| Net Income / (Loss) as reported | 170,612 | 24.4 | % 19.8 | % 142,387 | 22.3 % |
| Revised carrying value of convertible bond | 12,972 | | | | |
| Provision for R&D site transfer | | | | 18,316 | |
| Tax impact on provision for R&D site transfer | | | | (1,758) | |
| Adjusted Net Income | 183,584 | 26.3 | % 15.5 | % 158,945 | 24.9 % |
| Attributable to: | | | | | |
| Minority interest | 57 | | | 18 | |
| Equity holders of Serono S.A. | 183,527 | 26.3 | % 15.5 | % 158,927 | 24.9 % |

| Three months September 30 | Adjusted basis 2006 US\$ | Adjusted basis % change | Adjusted basis 2005 US\$ |
|---------------------------------|-----------------------------|----------------------------|-----------------------------|
| Basic Earnings per Share | | | |
| - Bearer shares | 12.52 | 14.8 | % 10.91 |
| - Registered shares | 5.01 | 14.8 | % 4.36 |
| - American depositary shares | 0.31 | 14.8 | % 0.27 |

Diluted Earnings per Share

| | | | |
|------------------------------|--------------|------|---------|
| - Bearer shares | 12.50 | 15.7 | % 10.80 |
| - Registered shares | 5.00 | 15.7 | % 4.32 |
| - American depositary shares | 0.31 | 15.7 | % 0.27 |

Adjusted net income and adjusted earnings per share are Non-IFRS financial measures and are not and should not be viewed as a substitute for IFRS reported net income and earnings per share. Non-IFRS financial measures are not standardized by IFRS and, therefore, have limits in its usefulness to investors and may not be comparable with the calculation of similar measures for other companies. Adjusted net income and adjusted earnings per share are an alternative view of performance used by management as they exclude those non-recurring, non-operational activities and transactions that are not necessarily relevant to understand the comparative operating performance of the company's underlying business for the period.

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Consolidated Balance Sheets (unaudited)

| As of | September 30, 2006 US\$ 000 | December 31, 2005 US\$ 000 |
|--|--------------------------------|-------------------------------|
| Assets | | |
| Current Assets | | |
| Cash and cash equivalents | 1,361,927 | 358,853 |
| Short-term available-for-sale financial assets | 397,524 | 565,545 |
| Trade accounts receivable | 467,550 | 402,358 |
| Inventories | 242,601 | 248,476 |
| Prepaid expenses and other current assets | 252,682 | 199,189 |
| Total Current Assets | 2,722,284 | 1,774,421 |
| Non-Current Assets | | |
| Tangible fixed assets | 819,691 | 746,430 |
| Intangible assets | 345,474 | 341,382 |
| Deferred tax assets | 222,427 | 224,779 |
| Investments in associates | 5,113 | 5,446 |
| Long-term available-for-sale financial assets | 471,011 | 736,543 |
| Other long-term assets | 55,498 | 92,234 |
| Total Non-Current Assets | 1,919,214 | 2,146,814 |
| Non-current assets classified as held for sale | 12,634 | |
| Total Assets | 4,654,132 | 3,921,235 |
| Liabilities | | |
| Current Liabilities | | |
| Trade and other payables | 386,252 | 343,525 |
| Short-term financial debts | 753,021 | 28,604 |
| Income taxes | 119,391 | 97,797 |
| Deferred income - current | 22,291 | 34,111 |
| Provisions - current | 35,529 | 29,291 |
| Other current liabilities | 165,514 | 183,396 |
| Total Current Liabilities | 1,481,998 | 716,724 |
| Non-Current Liabilities | | |
| Long-term financial debts | 16,923 | 635,039 |
| Deferred tax liabilities | 18,253 | 18,316 |
| Deferred income - non-current | 111,229 | 123,142 |
| Provisions - non-current | 126,803 | 108,607 |
| Other long-term liabilities | 134,968 | 148,465 |
| Total Non-Current Liabilities | 408,176 | 1,033,569 |
| Total Liabilities | 1,890,174 | 1,750,293 |
| Shareholders Equity | | |
| Share capital | 236,720 | 235,555 |
| Share premium | 533,982 | 500,605 |
| Treasury shares | (369,898) | (372,724) |
| Retained earnings | 2,270,311 | 1,803,929 |
| Fair value and other reserves | 70,012 | 14,654 |
| Cumulative foreign currency translation adjustments | 21,867 | (11,988) |
| Total Shareholders Equity attributable to equity holders of Serono S.A. | 2,762,994 | 2,170,031 |
| Minority Interests | 964 | 911 |
| Total Shareholders Equity | 2,763,958 | 2,170,942 |
| Total Liabilities and Shareholders Equity | 4,654,132 | 3,921,235 |

The accompanying selected explanatory notes form an integral part of these financial statements.

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Consolidated Statements of Changes in Equity (unaudited)

| | Share capital US\$ 000 | Share premium US\$ 000 | Treasury shares US\$ 000 | Retained earnings US\$ 000 | Fair value and other reserves US\$ 000 | Cumulative foreign currency translation adjustments US\$ 000 | Total Shareholders Equity attributable to Serono S.A. US\$ 000 | Minority interests US\$ 000 | Total Shareholders Equity US\$ 000 |
|--|---------------------------|---------------------------|-----------------------------|-------------------------------|--|---|---|--------------------------------|--|
| Balance as of January 1, 2005 | | | | | | | | | |
| As previously reported | 254,420 | 1,023,125 | (987,489) | 2,064,499 | 23,482 | 69,841 | 2,447,878 | 3,343 | 2,451,221 |
| Effect of adopting revised IAS 39 - Financial Instruments: Recognition and Measurement | | | | (28,547) | 33,347 | (2,245) | 2,555 | | 2,555 |
| Effect of adopting IFRS 2 - Share-Based Payment | | 15,875 | | (15,527) | | (348) | | | |
| Balance as of January 1, 2005 as restated | 254,420 | 1,039,000 | (987,489) | 2,020,425 | 56,829 | 67,248 | 2,450,433 | 3,343 | 2,453,776 |
| Fair value adjustments on available-for-sale investments taken to equity | | | | | (19,058) | | (19,058) | | (19,058) |
| Transferred to income statement on sale of available-for-sale investments | | | | | (31,945) | | (31,945) | | (31,945) |
| Transferred to income statement for impairment of available-for-sale investments | | | | | 8,486 | | 8,486 | | 8,486 |
| Fair value adjustments on cash flow hedge taken to equity | | | | | (9,180) | | (9,180) | | (9,180) |
| Transferred to income statements on fair value loss on interest rate swaps | | | | | 89 | | 89 | | 89 |
| Foreign currency translation effect | | | | | | (61,936) | (61,936) | | (61,936) |
| Net (loss) / income recognized directly in equity | | | | | (51,608) | (61,936) | (113,544) | | (113,544) |
| Net (loss) / income | | | | (250,257) | | | (250,257) | 778 | (249,479) |
| Total recognized income and expense | | | | (250,257) | (51,608) | (61,936) | (363,801) | 778 | (363,023) |
| Issue of share capital | 705 | 20,337 | 3,281 | | | | 24,323 | | 24,323 |

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| | | | | | | | | | | |
|---|----------------|----------------|-------------------|------------------|--------------|--------------|------------------|------------|--|------------------|
| Issue of call options on Serono shares | 262 | | | | | | 262 | | | 262 |
| Share-based compensation | 14,290 | | | | | | 14,290 | | | 14,290 |
| Cancellation of treasury shares | (20,001) | (591,338) | 611,339 | | | | | | | |
| Dividend - bearer shares | | | | (76,992) | | | (76,992) | | | (76,992) |
| Dividend - registered shares | | | | (33,390) | | | (33,390) | | | (33,390) |
| Purchase of minorities | | | | | | | | (3,152) | | (3,152) |
| Balance as of September 30, 2005 | 235,124 | 482,551 | (372,869) | 1,659,786 | 5,221 | 5,312 | 2,015,125 | 969 | | 2,016,094 |

The accompanying selected explanatory notes form an integral part of these financial statements.

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Consolidated Statements of Changes in Equity (unaudited)

| | Share capital US\$ 000 | Share premium US\$ 000 | Treasury shares US\$ 000 | Retained earnings US\$ 000 | Fair value and other reserves US\$ 000 | Cumulative foreign currency translation adjustments US\$ 000 | Total Shareholders Equity attributable to Serono S.A. US\$ 000 | Minority interests US\$ 000 | Total Shareholders Equity US\$ 000 |
|--|---------------------------|---------------------------|-----------------------------|-------------------------------|---|---|---|--------------------------------|---------------------------------------|
| Balance as of January 1, 2006 | 235,555 | 500,605 | (372,724) | 1,803,929 | 14,654 | (11,988) | 2,170,031 | 911 | 2,170,942 |
| Fair value adjustments on available-for-sale investments taken to equity | | | | | 60,998 | | 60,998 | | 60,998 |
| Transferred to income statement on sale of available-for-sale investments | | | | | (8,582) | | (8,582) | | (8,582) |
| Transferred to income statement for impairment of available-for-sale investments | | | | | 827 | | 827 | | 827 |
| Fair value adjustments on cash flow hedge taken to equity | | | | | 2,207 | | 2,207 | | 2,207 |
| Transferred to income statements on fair value gain on interest rate swaps | | | | | (94) | | (94) | | (94) |
| Serono share of equity recognized by associated companies | | | | | 2 | | 2 | | 2 |
| Foreign currency translation effect | | | | | | 33,855 | 33,855 | | 33,855 |
| Net income recognized directly in equity | | | | | 55,358 | 33,855 | 89,213 | | 89,213 |
| Net income | | | | 539,731 | | | 539,731 | 176 | 539,907 |
| Total recognized income and expense | | | | 539,731 | 55,358 | 33,855 | 628,944 | 176 | 629,120 |
| Issue of share capital | 1,165 | 33,377 | 2,826 | | | | 37,368 | | 37,368 |
| Share-based compensation | | | | 43,737 | | | 43,737 | | 43,737 |
| Dividend - bearer shares | | | | (35,224) | | | (35,224) | | (35,224) |
| Dividend - registered shares | | | | (81,862) | | | (81,862) | | (81,862) |
| Purchase of minorities | | | | | | | | (123) | (123) |
| Balance as of September 30, 2006 | 236,720 | 533,982 | (369,898) | 2,270,311 | 70,012 | 21,867 | 2,762,994 | 964 | 2,763,958 |

The accompanying selected explanatory notes form an integral part of these financial statements.

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Consolidated Statements of Cash Flows (unaudited)

| Nine months ended September 30 | 2006 US\$ 000 | 2005 US\$ 000 |
|---|------------------|------------------|
| Net Income / (Loss) | 539,907 | (249,479) |
| Reversal of non-cash items | | |
| Taxes | 89,355 | 10,290 |
| Depreciation and amortization | 95,554 | 100,911 |
| Interest income | (56,400) | (41,070) |
| Interest expense | 12,322 | 12,751 |
| Unrealized foreign currency exchange results | (4,000) | 1,190 |
| Legal provision | | 725,000 |
| Share of loss / (profit) of associates | 616 | (52) |
| Other non-cash items | 72,668 | (4,520) |
| Operating Cash Flows Before Working Capital Changes | 750,022 | 555,021 |
| Working capital changes | | |
| Trade and other payables, other current liabilities and deferred income | (15,985) | (65,911) |
| Trade accounts receivable and other receivables | (22,040) | 33,072 |
| Inventories | 25,975 | 5,806 |
| Prepaid expenses and other current assets | (47,493) | (1,548) |
| Taxes paid | (67,734) | (86,954) |
| Net Cash Flows From Operating Activities | 622,745 | 439,486 |
| Purchase of tangible fixed assets | (114,716) | (107,427) |
| Proceeds from disposal of tangible fixed assets | 2,326 | 2,374 |
| Purchase of intangible assets | (18,368) | (82,564) |
| Proceeds from disposal of intangibles | 400 | |
| Purchase of available-for-sale financial assets | | (248,508) |
| Proceeds from sale of available-for-sale financial assets | 485,826 | 685,182 |
| Purchase of investments in associates | | (4,721) |
| Interest received | 65,339 | 77,308 |
| Net Cash Flows From Investing Activities | 420,807 | 321,644 |
| Proceeds from issue of Serono shares | 11,218 | 11,055 |
| Proceeds from exercise of options on Serono shares | 20,447 | 6,418 |
| Proceeds from issue of call options on Serono shares | | 261 |
| Proceeds from issue of financial debts | 58,451 | 60,740 |
| Repayments of financial debt | (6,588) | (6,966) |
| Other non-current liabilities | (3,819) | (12,419) |
| Interest paid | (4,433) | (3,046) |
| Dividends paid | (117,086) | (110,382) |
| Net Cash Flows Used For Financing Activities | (41,810) | (54,339) |
| Effect of Exchange Rate Changes on Cash and Cash Equivalents | 1,332 | (1,461) |
| Net Increase in Cash and Cash Equivalents | 1,003,074 | 705,330 |
| Cash and Cash Equivalents at the Beginning of Period | 358,853 | 275,979 |
| Cash and Cash Equivalents at the End of Period | 1,361,927 | 981,309 |

The accompanying selected explanatory notes form an integral part of these financial statements.

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Selected explanatory notes to the interim financial report for the nine months ended September 30, 2006 (unaudited)**1. Basis of Preparation**

This unaudited interim financial report of the Serono group (group or Serono) has been prepared in accordance with IAS 34 - Interim Financial Reporting and in accordance with the accounting policies set out in the Serono 2005 Annual Report, with the exception of the following new International Financial Reporting Standards adopted by the group:

IAS 19 (Amended), Employee Benefits Actuarial Gains and Losses, Group Plans and Disclosures

The group has adopted the amendments to IAS 19, which introduces the option of an alternative recognition approach for actuarial gains and losses for defined benefit pension plans. The group has elected not to apply the option of recognizing actuarial gains and losses arising on its defined benefit plans in full in the statement of recognized income and expense and continues to recognize the amortization of actuarial gains and losses outside the corridor in the income statement.

The following amendments have been adopted by the group and have had no effect on these consolidated financial statements: IAS 39 (Amended), Cash Flow Hedge Accounting of Forecast Intragroup Transactions ; IAS 39 (Amended), The Fair Value Option ; IAS 39 and IFRS 4 (Amended), and Financial Guarantee Contracts .

These consolidated financial statements were approved for issuance on October 17, 2006 by Serono S.A.'s Board of Directors.

2. Segment information geographical segments

| Nine months ended September 30, 2006 | Western | North | Middle East, | Asia-Pacific, | Latin | Unallocated | Total |
|---|----------------|----------------|----------------|----------------|----------------|-------------|------------------|
| | Europe | America | Eastern | Oceania | America | | |
| | US\$000 | US\$000 | US\$000 | US\$000 | US\$000 | US\$000 | US\$000 |
| Product sales to third parties | 820,836 | 667,037 | 148,211 | 105,589 | 101,063 | | 1,842,736 |
| Royalty and license income | 175,734 | 2,707 | 44,519 | | | | 222,960 |
| Total revenues | 996,570 | 669,744 | 192,730 | 105,589 | 101,063 | | 2,065,696 |
| Operating income | 562,692 | 329,175 | 56,418 | 38,571 | 56,315 | (137,750) | 905,421 |
| Impairment losses on tangible and intangible assets | (576) | | | | | | (576) |
| Corporate research and development expenses | | | | | | (302,260) | (302,260) |
| Operating income | | | | | | | 602,585 |

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Selected explanatory notes to the interim financial report for the nine months ended September 30, 2006 (unaudited)

| Nine months ended September 30, 2005 | Western | North | Middle East, | Asia-Pacific, | Latin | Unallocated | Total |
|---|----------------|----------------|----------------|----------------|---------------|-------------|------------------|
| | Europe | America | Africa and | Oceania | America | | |
| | US\$000 | US\$000 | Europe | and Japan | US\$000 | US\$000 | US\$000 |
| Product sales to third parties | 783,472 | 617,376 | 139,550 | 100,874 | 93,100 | | 1,734,372 |
| Royalty and license income | 154,052 | 1,358 | 26,678 | | | | 182,088 |
| Total revenues | 937,524 | 618,734 | 166,228 | 100,874 | 93,100 | | 1,916,460 |
| Operating (loss) / income | (316,351 |) 322,470 | 43,753 | 31,252 | 49,761 | (75,310 |) 55,575 |
| Corporate research and development expenses | | | | | | (345,932 |) (345,932 |
| Operating loss | | | | | | | (290,357 |

Unallocated items represent income and expenses of corporate coordination functions, which are not directly attributable to specific geographical segments. Product sales to third parties are allocated to the geographical segments based on the country in which the customer is located. Royalty and license income is allocated to the geographical segments based on the country that receives the royalty. Operating income / (loss) is allocated to the geographical segments as recorded by the legal entities in the respective regions. There are no sales or other transactions between the geographical segments.

3. Financial income and expense

| Nine months ended September 30 | 2006 | 2005 |
|---|---------------|---------------|
| | US\$000 | US\$000 |
| Interest income | 56,400 | 41,070 |
| Other financial income | 511 | 27 |
| Fair value gain on interest rate swaps | 94 | |
| Realized gains on disposal of available-for-sale financial assets | 8,582 | 31,945 |
| Financial income | 65,587 | 73,042 |

| Nine months ended September 30 | 2006 | 2005 |
|--|------------------|------------------|
| | US\$000 | US\$000 |
| Interest expense | (12,322) | (12,751) |
| Other financial expense | (18,996) | (5,131) |
| Fair value loss on interest rate swaps | | (89) |
| Impairment losses on available-for-sale financial assets | (827) | (8,486) |
| Financial expense | (32,145) | (26,457) |

During the nine months ended September 30, 2006, the group recognized a realized gain of \$8.4 million (2005: \$30.0 million) on partial disposal of an available-for-sale equity investment and impairment losses of \$0.8 million (2005: \$8.4 million) on its available-for-sale equity investments.

Other financial expense includes a \$13.0 million charge relating to the revised carrying value of the 120,000 0.50% senior unsubordinated convertible bonds which was adjusted to reflect revised estimated cash flows due to the announced change of control, giving bondholders the right to put the bonds for cash.

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Selected explanatory notes to the interim financial report for the nine months ended September 30, 2006 (unaudited)

4. Taxes

The effective income tax rate for the nine months ended September 30, 2006 is 12.9% (2005: 12.4%). The effective income tax rate is calculated by dividing the income tax expense by the income / (loss) before taxes reduced by capital and other taxes, both without the tax impact of the litigation and related costs. Taxes recognized for the nine months ended September 30, 2005 included \$64.5 million in deferred tax income from the recognition of the litigation expense and related costs as disclosed in note 11 concerning legal proceedings.

| Nine months ended September 30 | 2006 | 2005 |
|--|---------------|---------------|
| | US\$000 | US\$000 |
| Income tax expense without tax impact for the litigation expense and related costs | 79,795 | 58,186 |
| Capital and other taxes | 9,560 | 16,629 |
| Total tax expense | 89,355 | 74,815 |
| Deferred tax income from litigation expense and related costs | | (64,525) |
| Total taxes | 89,355 | 10,290 |

5. Earnings / (loss) per share

Basic earnings / (loss) per share

Basic earnings / (loss) per share is calculated by dividing the net income /(loss) attributable to equity holders of Serono S.A. by the weighted average number of shares outstanding during the period presented. The number of outstanding shares is calculated by deducting the average number of shares purchased and held as treasury shares from the total number of issued shares.

| Nine months ended September 30 | 2006 | 2005 |
|--|----------------|-------------------|
| | US\$000 | US\$000 |
| Net income / (loss) attributable to bearer equity holders of Serono S.A. | 377,396 | (174,572) |
| Net income / (loss) attributable to registered equity holders of Serono S.A. | 162,335 | (75,685) |
| Total net income / (loss) attributable to the equity holders of Serono S.A. | 539,731 | (250,257) |
| Weighted average number of bearer shares outstanding | 10,241,279 | 10,160,991 |
| Weighted average number of registered shares outstanding | 11,013,040 | 11,013,040 |

| Nine months ended September 30 | 2006 | 2005 |
|--|-------|----------|
| | US\$ | US\$ |
| Basic earnings / (loss) per share | | |
| Bearer shares | 36.85 | (17.18) |
| Registered shares | 14.74 | (6.87) |
| American depository shares | 0.92 | (0.43) |

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Basis earnings per share for the three months ended September 30, 2006 was \$11.64 compared to \$9.77 for the three months ended September 30, 2005.

[more](#)

Selected explanatory notes to the interim financial report for the nine months ended September 30, 2006 (unaudited)**Diluted earnings / (loss) per share**

For diluted earnings / (loss) per share, the weighted average number of bearer shares outstanding is adjusted to assume conversion of all potential dilutive shares arising from outstanding stock options and the convertible bond. For stock options, a calculation is made to determine the number of shares that could have been acquired at fair value based on proceeds from the exercise of stock options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the stock options. The difference is added to the denominator as additional shares for no consideration. There is no adjustment made to the numerator. For the convertible bond, the number of shares into which the bond is assumed to be fully convertible is added to the denominator. The numerator is increased by eliminating the interest expense, net of tax that would not be incurred if the bond were converted. The effect of the convertible bond was excluded from the calculation of diluted earning per share for the nine months ended September 30, 2006 and 2005, as it was anti-dilutive. The effect of the outstanding stock options were excluded from the calculation of diluted earning per share for the nine months ended September 30, 2005, as they were anti-dilutive.

| Nine months ended September 30 | 2006 | 2005 |
|---|-------------------|----------------|
| | US\$000 | US\$000 |
| Net income / (loss) attributable to the equity holders of Serono S.A. for basic earnings / (loss) per share | 539,731 | (250,257) |
| Interest expense on convertible bond | | |
| Net income / (loss) attributable to the equity holders of Serono S.A. for dilutive earnings / (loss) per share | 539,731 | (250,257) |
| Weighted average number of bearer shares outstanding for basic earnings / (loss) per share | 10,241,279 | 10,160,991 |
| Adjustment for dilutive stock options | 33,099 | |
| Adjustment for assumed conversion of convertible bond | | |
| Weighted average number of bearer shares outstanding for dilutive earnings / (loss) per share | 10,274,378 | 10,160,991 |

| Nine months ended September 30 | 2006 | 2005 |
|--|--------------|-------------|
| | US\$ | US\$ |
| Diluted earnings / (loss) per share | | |
| Bearer shares | 36.77 | (17.18) |
| Registered shares | 14.71 | (6.87) |
| American depositary shares | 0.92 | (0.43) |

Fully diluted earnings per share for the three months ended September 30, 2006 was \$11.62 compared to \$9.70 for the three months ended September 30, 2005. Fully diluted earnings per share for the three months ended September 30, 2006 includes the dilutive impact of outstanding stock options that would result in the issuance of an additional 28,412 bearer shares. Fully diluted earnings per share for the three months ended September 30, 2005 includes the dilutive impact of outstanding stock options and the conversion of the convertible bond that would result in the issuance of an additional 457,570 bearer shares. The effect of the convertible bond was excluded from the calculation of Diluted Earnings per Share for the three months ended September 30, 2006 as it was anti-dilutive.

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Selected explanatory notes to the interim financial report for the nine months ended September 30, 2006 (unaudited)

6. Share capital

| Class of shares | As of September 30, 2006 | | | | |
|--|--------------------------|---------------|---------|----------------|----------------|
| | Number of shares | Nominal value | CHF000 | US\$000 | |
| Issued and fully paid share capital | | | | | |
| Registered | 11,013,040 | CHF10 | 110,130 | 68,785 | |
| Bearer | 10,891,790 | CHF25 | 272,295 | 167,935 | |
| Total | | | | 236,720 | |
| Authorized share capital | bearer | 9,018,860 | CHF25 | 225,472 | 179,601 |
| Conditional share capital and/or convertible bonds | bearer for options | 1,452,000 | CHF25 | 36,300 | 28,915 |
| Conditional share capital | bearer for stock options | 610,601 | CHF25 | 15,265 | 12,159 |

| Class of shares | As of December 31, 2005 | | | | |
|--|--------------------------|---------------|---------|---------|--------|
| | Number of shares | Nominal value | CHF000 | US\$000 | |
| Issued and fully paid share capital | | | | | |
| Registered | 11,013,040 | CHF10 | 110,130 | 68,785 | |
| Bearer | 10,832,507 | CHF25 | 270,813 | 166,770 | |
| Total | | | 380,943 | 235,555 | |
| Authorized share capital | bearer | 1,400,000 | CHF25 | 35,000 | 26,553 |
| Conditional share capital and/or convertible bonds | bearer for options | 1,452,000 | CHF25 | 36,300 | 27,540 |
| Conditional share capital | bearer for stock options | 669,884 | CHF25 | 16,747 | 12,705 |

Registered shares have a nominal value of CHF10 each and bearer shares have a nominal value of CHF25 each. Registered and bearer shares participate in dividends in proportion to their nominal value. Each share entitles the holder to one vote. The authorized share capital may be used by Serono S.A. or its affiliates to finance research and development projects and acquire interests in other companies.

The shareholders at the Annual General Meeting of Shareholders on April 25, 2006 authorized an increase in share capital by a maximum amount of CHF190,471,500 through the issuance of a maximum of 7,618,860 new bearer shares, each with a par value of CHF25, until April 25, 2008. The Board of Directors may proceed to increase the share capital all at once or in installments.

7. Treasury shares

There were 641,470 treasury shares held by the group as of January 1, 2006. During the nine months ended September 30, 2006, no additional treasury shares were acquired (none in 2005). During the nine months ended September 30, 2006, 5,392 treasury shares were granted to employees (6,221 shares in 2005) as part of the Employee Share Purchase Plan. In addition, 29 treasury shares were issued as part of the Stock Grant Plan, 233 treasury shares were issued as part of the Restricted Share Plan and no additional treasury shares (988 shares in 2005) were issued upon the exercise of stock options as part of the Director Stock Option Plan. The total number of treasury shares held as of September 30, 2006 is 635,816.

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Selected explanatory notes to the interim financial report for the nine months ended September 30, 2006 (unaudited)

8. Distribution of earnings

The proposed gross dividend in respect of 2005 of CHF4.00 gross (2005: CHF3.60) per registered share, CHF10.00 gross (2005: CHF9.00) per bearer share or CHF0.25 gross (2004: CHF0.23) per American depository share, was approved by shareholders at the Serono Annual General Meeting held on April 25, 2006. The dividend equivalent to \$117.1 million was subsequently paid on April 28, 2006 and has been accounted for as an appropriation of retained earnings in the nine months ended September 30, 2006.

9. Equity compensation plans**Employee Stock Option Plan**

Stock options are granted to senior management members of Serono S.A. and its affiliates. Each stock option gives the holder the right to purchase one bearer share or one American depository share (ADS) of Serono S.A. stock, depending on which affiliate employs the holder. Stock options are granted every plan year and vest as follows: 25% one year after date of grant, 50% after two years, 75% after three years and 100% after four years. Options expire six years after the fourth and final vesting date such that each option has a 10-year duration. The exercise price is equal to the fair market value of the underlying Serono S.A. bearer share or American depository shares on the date of grant. Movements in the number of employee bearer stock options and ADS stock options outstanding are as follows:

| | 2006 | Weighted average exercise price CHF | 2005 | Weighted average exercise price CHF |
|---------------------------------------|-------------------|--|-------------------|--|
| | Bearer options | | Bearer options | |
| Outstanding as of January 1 | 382,692 | 984 | 346,486 | 995 |
| Granted | 104,620 | 916 | 92,625 | 858 |
| Exercised | (32,388) | 721 | (11,130) | 631 |
| Cancelled | (31,691) | 1,098 | (19,827) | 1,103 |
| Outstanding as of September 30 | 423,233 | 979 | 408,154 | 968 |

| | 2006 | Weighted average exercise price US\$ | 2005 | Weighted average exercise price US\$ |
|---------------------------------------|------------------|---|------------------|---|
| | ADS options | | ADS options | |
| Outstanding as of January 1 | 1,791,150 | 16.52 | 1,066,800 | 15.54 |
| Granted | 902,720 | 17.49 | 979,000 | 17.46 |
| Exercised | (127,650) | 15.86 | (14,550) | 15.55 |
| Cancelled | (229,990) | 17.02 | (196,450) | 16.00 |
| Outstanding as of September 30 | 2,336,230 | 16.88 | 1,834,800 | 16.52 |

During the nine months ended September 30, 2006, 32,388 bearer stock options (2005: 11,130 bearer stock options) were exercised yielding proceeds of CHF23.4 million or \$18.4 million (2005: CHF7.0 million or \$5.7 million) and 127,650 ADS options (2005: 14,550 options) were exercised yielding proceeds of \$2.0 million (2005: \$0.2 million). Bearer and ADS stock options cancelled in all years since inception of the plan are the result of options forfeited by participants upon their departure from the group. The total number of bearer and ADS stock options available for grant as of September 30, 2006 is 102,922 options (2005: 216,383 options).

Director Stock Option Plan

Stock options are granted to members of the Board of Directors of Serono S.A. Each stock option gives the holder the right to purchase one bearer share of Serono S.A. stock. Stock options are granted every plan year and vest beginning

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Selected explanatory notes to the interim financial report for the nine months ended September 30, 2006 (unaudited)

one year after their grant rateably over four years. Each option has a 10-year duration. The exercise price is equal to the fair market value of the underlying Serono S.A. bearer share on the date of grant. There were 5,200 options granted (2005: 5,200) to directors during the nine months ended September 30, 2006. No director stock options were cancelled or exercised (1,320 options were exercised in 2005, yielding total proceeds of CHF0.7 million or \$0.5 million) during the nine months ended September 30, 2006. There are 27,000 director stock options outstanding as of September 30, 2006 (2005: 23,850 director stock options) with a weighted average exercise price of CHF798 (2005: CHF771).

A total compensation expense of \$17.2 million (2005: \$13.8 million) has been recognized for the nine months ended September 30, 2006 arising on share-based payment transactions related to stock options. The compensation expense in 2006 has been charged to the appropriate income statement headings as follows: cost of product sales \$1.3 million, selling, general and administrative \$9.2 million and research and development \$6.7 million.

Employee Share Purchase Plan

The group has an Employee Share Purchase Plan (ESPP) covering substantially all of its employees. The ESPP is designed to allow employees to purchase every calendar year bearer shares or American depositary shares at 85% of the lower of the average market values in the 10 days preceding the beginning and end of the calendar year. Shares purchased under the ESPP are granted in January of the following calendar year. Purchases under the ESPP are subject to certain restrictions and may not exceed 15% of the employee's annual salary. During the nine months ended September 30, 2006, 21,904 bearer shares (2005: 20,940 bearer shares) were issued to employees at a price of CHF630 per share (2005: CHF630 per share). As of September 30, 2006, a total of \$8.5 million (2005: \$8.5 million) in contributions was held by the group to be used to purchase bearer and American depositary shares on behalf of employees in January 2007.

Shares purchased under the ESPP that are held for one calendar year after the purchase date entitle each participant to receive, on a one-time basis in early January of each year, one matching share for every three shares purchased and held. In January 2006, 5,437 bearer shares (2005: 5,766 bearer shares) were distributed to employees.

The total compensation expense of \$6.2 million (2005: \$5.6 million) has been recognized for the nine months ended September 30, 2006 arising on share-based payment transactions related to the ESPP discount and matching shares. The compensation expense in 2006 has been charged to the appropriate income statement headings as follows: cost of product sales \$1.1 million, selling, general and administrative \$3.4 million and research and development \$1.7 million.

Director Share Purchase Plan

The group has a share purchase plan reserved for its Board of Directors (the DSPP). The DSPP allows board members to purchase Serono S.A. bearer shares through allocation of 50% or 100% of their gross yearly fees. Each cycle commences on the first business day following the Annual General Meeting of Shareholders (the AGM) and concludes on the day of the next AGM. Directors must elect to participate in the DSPP at the beginning of each cycle. The purchase price per share is 85% of the fair market value of the share on the fifth business day following the AGM. Shares are purchased at the end of each cycle. There were 1,800 bearer shares issued to the directors that participate in the plan during the first nine months of 2006 (1,348 in 2005).

Restricted Share Plan

The group has a Restricted Share Plan whereby employees may be granted restricted share awards as a result of an award based on certain performance criteria. Shares granted under this plan generally have a three-year vesting period. No shares were granted to employees during the first nine months of 2006 and 2005.

Stock Grant Plan

The group adopted a new Stock Grant Plan effective January 1, 2006, whereby selected employees may be granted restricted share awards at the absolute discretion of the Board of Directors. Shares granted under this plan will vest in three annual installments on the first, second and third anniversaries of the grant date subject to continuous employment from the grant date to the vesting dates. There were 29,388 bearer shares and 797,126 American depositary shares granted to selected employees during the first nine months of 2006. The compensation expense in

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Selected explanatory notes to the interim financial report for the nine months ended September 30, 2006 (unaudited)

2006 of \$12.9 million has been charged to the appropriate income statement headings as follows: cost of product sales \$0.9 million, selling, general and administrative \$7.7 million and research and development \$4.3 million.

10. Principal shareholders

As of September 30, 2006, Bertarelli Biotech S.A., a corporation with its principal offices at Chésereux (Vaud), Switzerland, held 56.96% of the capital and 66.89% of the voting rights in Serono S.A. Ernesto Bertarelli controls Bertarelli Biotech S.A. On the same date, Maria-Iris Bertarelli, Ernesto Bertarelli and Donata Bertarelli Späth owned in the aggregate 4.77% of the capital and 8.57% of the voting rights of Serono S.A.

On September 21, 2006, Maria-Iris Bertarelli, Ernesto Bertarelli and Donata Bertarelli Späth agreed to sell all the shares of Bertarelli Biotech S.A. and all the registered shares of Serono S.A. that they hold to a subsidiary of Merck KGaA, a German company. The sale is subject to conditions precedent usual for this type of transaction, including the receipt of antitrust clearances, and will be consummated on January 3, 2007 at the earliest. After consummation of the sale, Maria-Iris Bertarelli, Ernesto Bertarelli and Donata Bertarelli Späth will hold less than 5% of the voting rights of Serono S.A.

11. Legal proceedings

Serono's principal US subsidiary, Serono Inc., received a subpoena in 2001 from the US Attorney's office in Boston, Massachusetts requesting that it produce documents for the period from 1992 forward relating to Serostim. During 2002, Serono Inc. also received subpoenas from the states of California, Florida, Maryland and New York, which mirror the requests in the US Attorney's subpoena. Other pharmaceutical companies have received similar subpoenas as part of an ongoing, industry-wide investigation by the states and the federal government into sales, marketing and other practices. These investigations seek to determine whether such practices violated any laws, including the Federal False Claims Act or the US Food, Drug and Cosmetic Act or constituted fraud in connection with Medicare and/or Medicaid reimbursement to third parties. Serono cooperated fully with the investigation and agreed to settle this dispute in October 2005. Under the terms of the settlement agreement, approximately \$724.9 million was paid as a comprehensive settlement with federal and state governments and to cover related costs. Serono's US holding company, Serono Holding Inc., also entered into a Corporate Integrity Agreement with the Office of Inspector General of the US Department of Human Health Services in connection with the investigation.

In September 2005, the Government Employees Hospital Association (GEHA), a health insurance plan, filed a purported class action on behalf of third party payors and individual consumers against Serono Inc. and Serono International S.A. alleging that Serono Inc. and Serono International S.A. inflated the average wholesale price (AWP) of certain products, and that this inflation caused GEHA to overpay for those products. In November 2005, GEHA filed an amended complaint alleging, in addition to its average wholesale price claims, that Serono illegally promoted and marketed Serostim. In February 2006, GEHA requested (and Serono consented to) permission from the court to file a Second Amended Class Action Complaint which adds another plaintiff, District Council 37 Health & Security Plan Trust (alleged to be a third party payor of prescriptions for its members), does not contain any AWP claims, adds Serono Laboratories, Inc. as a defendant, alleges that Serono illegally promoted and marketed Serostim, and alleges that Serono used improper and inappropriate sales and marketing practices to increase the sales of other Serono products, including Cetrotide, Crinone, Gonal-F, Fertinex, Ovidrel, Pergonal, Profasi, Rebif, and Saizen. In October 2006, GEHA filed a Third Amended Complaint that adds another Plaintiff, Health Net, Inc., and eliminates claims with respect to products other than Serostim. The allegations in the Third Amended Complaint concerning Serostim are drawn from the government investigation of Serostim discussed above. The Third Amended Complaint alleges eight counts: (1) violation of 18 U.S.C. § 1962(C) (civil RICO); (2) violation of 18 U.S.C. § 1962(C) (civil RICO); (3) violation of 18 U.S.C. § 1962(D) (civil RICO conspiracy); (4) civil conspiracy; (5) violation of the Massachusetts Consumer Protection Act; (6) violation of consumer protection statutes of 44 states and the District of Columbia; (7) common law fraud; and (8) unjust enrichment. The Serono Defendants have not yet filed an answer.

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Selected explanatory notes to the interim financial report for the nine months ended September 30, 2006 (unaudited)

In April 2006, Eugene Francis filed a purported class action on behalf of all persons or entities that paid a portion of the purchase price for Serostim against Serono Inc., Serono Laboratories, Inc., and certain other parties. The allegations of the complaint concern only the sales and marketing of Serostim, and are substantially similar to the allegations concerning Serostim made in the GEHA matter described above. The complaint contains the same eight counts as the GEHA Second Amended Complaint described above. The Serono Defendants have not yet filed an answer. The case has been consolidated with the GEHA case.

The Serono Defendants intend to vigorously defend the GEHA and Francis cases. In October 2006, the GEHA and Francis Plaintiffs made an offer to settle the Serostim portion of the case. The company intends to engage in settlement discussions with the GEHA and Francis Plaintiffs. However, there is no assurance that such discussions will lead to a settlement or the ultimate amount or other terms of any settlement. The final settlement or adjudication of these cases could have a material adverse effect on the operations or financial condition of the company. The company cannot predict the timing of the resolution of these cases or ultimate outcome.

end

SIGNATURE

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.

SERONO
S.A.,
a Swiss corporation
(Registrant)

Date October 19, 2006

By: /s/ Stuart Grant
Name: Stuart Grant
Title: Chief Financial Officer
