UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q/A

(Amendment No. 2)

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

For the quarterly period ended March 31, 2004

¨ **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 1-4448

BAXTER INTERNATIONAL INC.

(Exact name of registrant as specified in its charter)

Delaware	**36-0781620**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
One Baxter Parkway, Deerfield, Illinois	**60015-4633**
(Address of principal executive offices)	**(Zip Code)**

(847) 948-2000

(Registrant s telephone number, including area code)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes x No ¨

The number of shares of the registrant s Common Stock, par value $1.00 per share,

outstanding as of March 28, 2005 was 619,758,508 shares.

EXPLANATORY NOTE

Baxter International Inc. is filing this Form 10-Q/A Amendment No. 2 for the quarter ended March 31, 2004 to reflect the restatement of its consolidated financial statements for the quarters ended March 31, 2004 and 2003. The restatement arises from the controls surrounding the income tax accounts. Specifically, current income taxes payable balances were not reconciled to expected tax payments due, and the company did not adequately review the difference between the income tax basis and the financial reporting basis of assets and liabilities, and reconcile the difference to recorded deferred income tax assets and liabilities. Refer to Note 1B for a complete description and quantification of the restatement. Also, refer to Note 1A regarding the company s previous restatement of its consolidated financial statements for the quarters ended March 31, 2004 and 2003, filed as Form 10-Q/A Amendment No. 1.

The information in this Form 10-Q/A Amendment No. 2 has not been updated from the Form 10-Q or Form 10-Q/A Amendment No. 1 except as required to reflect the effects of the restatement. This restatement includes changes to Part I, Items 1, 2 and 4. Items included in the original Form 10-Q that are not included herein are not amended and remain in effect as of the date of the original filing. Additionally, this Form 10-Q/A Amendment No. 2 does not purport to provide an update or a discussion of any other developments at the company subsequent to the original filing.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Baxter International Inc. and Subsidiaries

Condensed Consolidated Statements of Income (unaudited)

(in millions, except per share data)

	Restated	
	Three months ended March 31,	
	2004	**2003**
Net sales	$2,209	$1,995
Costs and expenses		
Cost of goods sold	1,316	1,117
Marketing and administrative expenses	466	414
Research and development expenses	136	136
Net interest expense	21	19
Other expense, net	21	26
Total costs and expenses	1,960	1,712
Income from continuing operations before income taxes	249	283
Income tax expense	62	68
Income from continuing operations	187	215
Discontinued operations	(11)	(1)
Net income	$ 176	$ 214
Earnings per basic common share		
Continuing operations	$ 0.31	$ 0.36
Discontinued operations	(0.02)	
Net income	$ 0.29	$ 0.36
Earnings per diluted common share		
Continuing operations	$ 0.30	$ 0.36
Discontinued operations	(0.02)	(0.01)
Net income	$ 0.28	$ 0.35
Weighted average number of common shares outstanding		

Basic	612	598
Diluted	616	611

The accompanying notes are an integral part of these condensed consolidated financial statements.

Baxter International Inc. and Subsidiaries

Condensed Consolidated Balance Sheets (unaudited)

(in millions, except shares)

	Restated	
	March 31, 2004	**December 31, 2003**
Current assets		
Cash and equivalents	$ 646	$ 925
Accounts and other current receivables	2,029	1,914
Inventories	2,168	2,104
Short-term deferred income taxes	209	140
Prepaid expenses and other	268	277
Total current assets	5,320	5,360
Property, plant and equipment		
At cost	7,825	7,791
Accumulated depreciation and amortization	(3,265)	(3,199)
Net property, plant and equipment	4,560	4,592
Other assets		
Goodwill	1,599	1,599
Other intangible assets	605	611
Other	1,570	1,545
Total other assets	3,774	3,755
Total assets	$13,654	$13,707
Current liabilities		
Short-term debt	$ 177	$ 153
Accounts payable and accrued liabilities	2,533	3,107
Income taxes payable	443	438
Total current liabilities	3,153	3,698
Long-term debt and lease obligations	4,630	4,421
Other long-term liabilities	2,279	2,206
Commitments and contingencies		
Stockholders equity		
Common stock, $1 par value, authorized 2,000,000,000 shares, issued 648,574,109 shares in 2004 and 2003	649	649
Common stock in treasury, at cost, 36,110,243 shares in 2004 and 37,273,424 shares in 2003	(1,799)	(1,863)
Additional contributed capital	3,741	3,786
Retained earnings	2,406	2,230

Accumulated other comprehensive loss	(1,405)	(1,420)
Total stockholders equity	3,592	3,382
Total liabilities and stockholders equity	$13,654	$13,707

The accompanying notes are an integral part of these condensed consolidated financial statements.

Baxter International Inc. and Subsidiaries

Condensed Consolidated Statements of Cash Flows (unaudited)

(in millions)

	Restated	
	Three months ended March 31,	
(brackets denote cash outflows)	**2004**	**2003**
Cash flows from operations		
Income from continuing operations	$ 187	$ 215
Adjustments		
Depreciation and amortization	149	128
Deferred income taxes	10	(70)
Other	23	8
Changes in balance sheet items		
Accounts receivable	(96)	(53)
Inventories	(66)	(134)
Accounts payable and accrued liabilities	(252)	(79)
Restructuring payments	(37)	(7)
Other	29	(30)
Cash flows from continuing operations	(53)	(22)
Cash flows from discontinued operations	(1)	(6)
Cash flows from operations	(54)	(28)
Cash flows from investing activities		
Capital expenditures	(90)	(175)
Acquisitions (net of cash received) and investments in and advances to affiliates	(14)	(71)
Divestitures and other	26	
Cash flows from investing activities	(78)	(246)
Cash flows from financing activities		
Issuances of debt	87	610
Redemptions of debt and lease obligations	(33)	(119)
Increase in debt with maturities of three months or less, net	137	527
Common stock cash dividends	(361)	(346)
Proceeds from stock issued under employee benefit plans	31	16
Purchases of treasury stock	(11)	(153)
Cash flows from financing activities	(150)	535
Effect of currency exchange rate changes on cash and equivalents	3	(22)
Increase (decrease) in cash and equivalents	(279)	239
Cash and equivalents at beginning of period	925	1,169

Cash and equivalents at end of period	$ 646	$1,408

The accompanying notes are an integral part of these condensed consolidated financial statements.

Baxter International Inc. and Subsidiaries

Notes to Condensed Consolidated Financial Statements (unaudited)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The unaudited interim condensed consolidated financial statements of Baxter International Inc. and its subsidiaries (the company or Baxter) have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. These interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the company s 2003 Annual Report to Stockholders (2003 Annual Report).

In the opinion of management, the interim condensed consolidated financial statements reflect all adjustments necessary for a fair presentation of the interim periods. All such adjustments, unless otherwise noted herein, are of a normal, recurring nature. The results of operations for the interim period are not necessarily indicative of the results of operations to be expected for the full year.

Certain reclassifications have been made to conform the 2003 financial statements and notes to the 2004 presentation.

Stock compensation plans

The company has a number of stock-based employee compensation plans, including stock option, stock purchase and restricted stock plans. The company applies the recognition and measurement principles of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations in accounting for these plans. In accordance with this intrinsic value method, no compensation expense is recognized for the company s fixed stock option plans and employee stock purchase plans. The following table illustrates the effect on net income and earnings per share (EPS) if the company had applied the fair value recognition provisions of Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation, to all stock-based employee compensation.

	Restated	
	Three months ended March 31,	
(in millions, except per share data)	**2004**	**2003**
Net income, as reported	$ 176	$ 214
Add: Stock-based employee compensation expense included in reported net income, net of tax		
Deduct: Total stock-based employee compensation expense determined under the fair value method, net of tax	28	37
Pro forma net income	$ 148	$ 177

Earnings per basic share		
As reported	$0.29	$0.36
Pro forma	$0.25	$0.30
Earnings per diluted share		
As reported	$0.28	$0.35
Pro forma	$0.23	$0.29

Changes in accounting principles

Financial Accounting Standards Board (FASB) Interpretation No. 46, Consolidation of Variable Interest Entities (FIN 46) was adopted July 1, 2003. Refer to the 2003 Annual Report for further information. In December 2003, the FASB revised and reissued FIN 46 (FIN 46-R). The provisions of FIN 46-R were required to be adopted no later than March 31, 2004. Baxter adopted FIN 46-R on March 31, 2004, and adoption of the revised standard did not have a material impact on the company s consolidated financial statements.

1A. RESTATEMENT OF PREVIOUSLY ISSUED CONSOLIDATED FINANCIAL STATEMENTS AMENDMENT No. 1

The company has restated its previously issued financial statements for 2001 through 2003 and the first quarter of 2004, primarily the result of the inappropriate application of accounting principles for revenue recognition and inadequate provisions for bad debts in Brazil during the period. Specifically, the company has restated previously issued financial information for 2001 through 2003 contained in its previously filed Forms 10-K for the years ended December 31, 2003, 2002 and 2001 by filing a Form 10-K/A Amendment No. 1 for the year ended December 31, 2003. The company s previously reported quarterly information in its Forms 10-Q for the quarters ended March 31, 2004, September 30, 2003, June 30, 2003 and March 31, 2003 have also been restated by filing a Form 10-Q for the quarter ended June 30, 2004 and a Form 10-Q/A Amendment No. 1 for each of the quarters ended March 31, 2004 and September 30, 2003. As a result of the restatement, in aggregate, net sales decreased $37 million (0.2% of the originally reported amount) and net income decreased $33 million (1.5% of the originally reported amount) over the three-year period ended December 31, 2003.

The following is a summary of the impact of the restatement on the previously issued consolidated income statements and consolidated balance sheets included in this filing. For the first quarter of 2004, net sales were unchanged as a result of the restatement and net income decreased $2 million (1.1% of the originally reported amount). For the first quarter of 2003, net sales decreased $2 million (0.1% of the originally reported amount) and net income decreased $2 million (0.9% of the originally reported amount).

Consolidated Statements of Income for the Three Months Ended March 31, 2004 and 2003

	Three months ended March 31,			
	2004		2003	
(in millions, except per share data)	**As originally reported**	**As restated**	**As originally reported**	**As restated**
Net sales	$2,209	$2,209	$1,997	$1,995
Costs and expenses				
Cost of goods sold	1,315	1,316	1,117	1,117
Marketing and administrative expenses	464	466	413	414
Research and development expenses	136	136	136	136
Net interest expense	21	21	19	19
Other expense, net	21	21	26	26
Total costs and expenses	1,957	1,960	1,711	1,712
Income from continuing operations before income taxes	252	249	286	283

Income tax expense	63	62	69	68
Income from continuing operations	189	187	217	215
Discontinued operations	(11)	(11)	(1)	(1)
Net income	$ 178	$ 176	$ 216	$ 214
Earnings per basic common share				
Continuing operations	$ 0.31	$ 0.31	$ 0.36	$ 0.36
Discontinued operations	(0.02)	(0.02)		
Net income	$ 0.29	$ 0.29	$ 0.36	$ 0.36
Earnings per diluted common share				
Continuing operations	$ 0.31	$ 0.30	$ 0.36	$ 0.36
Discontinued operations	(0.02)	(0.02)	(0.01)	(0.01)
Net income	$ 0.29	$ 0.28	$ 0.35	$ 0.35

Consolidated Balance Sheets at March 31, 2004 and December 31, 2003

(in millions, except shares)	March 31, 2004		December 31, 2003	
	As originally reported	As restated	As originally reported	As restated
Current assets				
Cash and equivalents	$ 648	$ 646	$ 927	$ 925
Accounts and other current receivables	2,097	2,029	1,979	1,914
Inventories	2,166	2,168	2,101	2,104
Short-term deferred income taxes	209	209	140	140
Prepaid expenses and other	280	268	290	277
Total current assets	5,400	5,320	5,437	5,360
Property, plant and equipment				
At cost	7,815	7,825	7,781	7,791
Accumulated depreciation and amortization	(3,261)	(3,265)	(3,196)	(3,199)
Net property, plant and equipment	4,554	4,560	4,585	4,592
Other assets				
Goodwill	1,648	1,648	1,648	1,648
Other intangible assets	605	605	611	611
Other	1,523	1,523	1,498	1,498
Total other assets	3,776	3,776	3,757	3,757
Total assets	$13,730	$13,656	$13,779	$13,709
Current liabilities				
Short-term debt	$ 177	$ 177	$ 153	$ 153
Accounts payable and accrued liabilities	2,532	2,533	3,105	3,107
Income taxes payable	567	543	561	538
Total current liabilities	3,276	3,253	3,819	3,798
Long-term debt and lease obligations	4,630	4,630	4,421	4,421
Other long-term liabilities	2,289	2,289	2,216	2,216
Commitments and contingencies				
Stockholders equity				
Common stock, $1 par value, authorized 2,000,000,000 shares, issued 648,574,109 shares in 2004 and 2003	649	649	649	649
Common stock in treasury, at cost, 36,110,243 shares in 2004 and 37,273,424 shares in 2003	(1,799)	(1,799)	(1,863)	(1,863)
Additional contributed capital	3,728	3,728	3,773	3,773
Retained earnings	2,372	2,321	2,194	2,145
Accumulated other comprehensive loss	(1,415)	(1,415)	(1,430)	(1,430)
Total stockholders equity	3,535	3,484	3,323	3,274

Total liabilities and stockholders equity	$13,730	$13,656	$13,779	$13,709

Senior management became aware of these issues in 2004 through the reporting procedures established under Baxter s Global Business Practice Standards. Upon becoming aware of the issues in Brazil, senior management, with the assistance of the company s internal audit team, conducted a preliminary investigation. This preliminary investigation was followed by a more comprehensive investigation by the Audit Committee of Baxter s Board of Directors with the assistance of independent legal counsel and forensic and other accountants. As a result of the issues in Brazil, the company has implemented changes to its internal control over financial reporting. Refer to Item 4. Controls and Procedures for further information.

1B. RESTATEMENT OF PREVIOUSLY ISSUED CONSOLIDATED FINANCIAL STATEMENTS AMENDMENT No. 2

The company has restated its previously issued financial statements for 2001 through 2003 and the first three quarters of 2004 as a result of inadequate reconciliations, leading to classification errors in tax and other related balance sheet accounts. Specifically, the company restated previously issued financial information contained in its Form 10-K/A Amendment No. 1 for the years ended December 31, 2003, 2002 and 2001 by filing a Form 10-K/A Amendment No. 2 for the year ended December 31, 2003. The company s previously reported quarterly information in its Form 10-Q/A Amendment No. 1 for the quarter ended March 31, 2004 has been restated by filing this Form 10-Q/A Amendment No. 2 for the quarter ended March 31, 2004. The company s previously reported quarterly information in its Forms 10-Q for the quarters ended June 30, 2004 and September 30, 2004 has been restated by filing a Form 10-Q/A Amendment No. 1 for each of the quarters ended June 30, 2004 and September 30, 2004.

As a result of the restatement, stockholders equity as of both March 31, 2004 and December 31, 2003 increased approximately $108 million, with offsetting decreases of approximately $157 to net tax liabilities and $49 million to goodwill. The restatement did not impact the consolidated statements of income or cash flows for the quarters ended March 31, 2004 and 2003.

The following is a summary of the impact of the restatement on the previously filed (Form 10-Q/A Amendment No. 1) consolidated balance sheets at March 31, 2004 and December 31, 2003.

Consolidated Balance Sheets at March 31, 2004 and December 31, 2003

	March 31, 2004		December 31, 2003	
(in millions, except shares)	**As previously reported (Amendment No. 1)**	**As restated**	**As previously reported (Amendment No. 1)**	**As restated**
Current assets				
Cash and equivalents	$ 646	$ 646	$ 925	$ 925
Accounts and other current receivables	2,029	2,029	1,914	1,914
Inventories	2,168	2,168	2,104	2,104
Short-term deferred income taxes	209	209	140	140
Prepaid expenses and other	268	268	277	277
Total current assets	5,320	5,320	5,360	5,360
Property, plant and equipment				
At cost	7,825	7,825	7,791	7,791
Accumulated depreciation and amortization	(3,265)	(3,265)	(3,199)	(3,199)
Net property, plant and equipment	4,560	4,560	4,592	4,592
Other assets				
Goodwill	1,648	1,599	1,648	1,599
Other intangible assets	605	605	611	611
Other	1,523	1,570	1,498	1,545
Total other assets	3,776	3,774	3,757	3,755
Total assets	$13,656	$13,654	$13,709	$13,707
Current liabilities				
Short-term debt	$ 177	$ 177	$ 153	$ 153
Accounts payable and accrued liabilities	2,533	2,533	3,107	3,107
Income taxes payable	543	443	538	438

Total current liabilities	3,253	3,153	3,798	3,698
Long-term debt and lease obligations	4,630	4,630	4,421	4,421
Other long-term liabilities	2,289	2,279	2,216	2,206
Commitments and contingencies				
Stockholders equity				
Common stock, $1 par value, authorized 2,000,000,000 shares, issued 648,574,109 shares in 2004 and 2003	649	649	649	649
Common stock in treasury, at cost, 36,110,243 shares in 2004 and 37,273,424 shares in 2003	(1,799)	(1,799)	(1,863)	(1,863)
Additional contributed capital	3,728	3,741	3,773	3,786
Retained earnings	2,321	2,406	2,145	2,230
Accumulated other comprehensive loss	(1,415)	(1,405)	(1,430)	(1,420)
Total stockholders equity	3,484	3,592	3,274	3,382
Total liabilities and stockholders equity	$13,656	$13,654	$13,709	$13,707

2. SUPPLEMENTAL FINANCIAL INFORMATION

Net interest expense

Net interest expense consisted of the following.

	Three months ended March 31,	
(in millions)	**2004**	**2003**
Interest expense	$ 28	$ 30
Interest income	(7)	(10)
Interest expense, net	$ 21	$ 20
Continuing operations	$ 21	$ 19
Discontinued operations	$	$ 1

Other income and expense

Other income and expense generally includes amounts relating to fluctuations in currency exchange rates, minority interests, income and losses relating to equity method investments, divestitures gains and asset impairment charges. Other expense for the three months ended March 31, 2003 included a pre-tax impairment charge totaling $13 million, relating to an investment whose decline in value was deemed to be other than temporary, with the investment written down to its market value, as determined by reference to quoted market prices.

Comprehensive income

Total comprehensive income was $191 million (as restated) and $183 million (as restated) for the three months ended March 31, 2004 and 2003, respectively. The increase in comprehensive income during 2004 was principally related to favorable movements in the company s foreign currency hedges, partially offset by reduced net income and unfavorable currency translation adjustments.

Earnings per share

The numerator for both basic and diluted EPS is net earnings available to common shareholders. The denominator for basic EPS is the weighted-average number of common shares outstanding during the period. The dilutive effect of outstanding employee stock options, employee stock purchase subscriptions and the purchase contracts in the company s equity units is reflected in the denominator for diluted EPS by

application of the treasury stock method under SFAS No. 128, Earnings per Share. Prior to the adoption of SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity,

on July 1, 2003, the dilutive effect of equity forward agreements was reflected in the denominator for diluted EPS by application of the reverse treasury stock method. Refer to the 2003 Annual Report for additional information regarding the company s equity units (which did not have a dilutive effect in either 2004 or 2003), as well as the equity forward agreements (which were terminated during the third quarter of 2003). The following is a reconciliation of the shares (denominator) of the basic and diluted per-share computations.

	Three months ended March 31,	
(in millions)	**2004**	**2003**
Basic shares	612	598
Effect of dilutive securities		
Employee stock options	2	1
Equity forward agreements		10
Employee stock purchase plans	2	2
Diluted shares	616	611

Inventories

Inventories consisted of the following.

	Restated	
(in millions)	**March 31, 2004**	**December 31, 2003**
Raw materials	$ 540	$ 568
Work in process	743	731
Finished products	885	805
Total inventories	$2,168	$2,104

Goodwill

Goodwill was $863 million (as restated), $569 million (as restated) and $167 million (as restated) for the Medication Delivery, BioScience and Renal segments, respectively, at March 31, 2004. Goodwill was $860 million (as restated), $571 million (as restated) and $168 million (as restated) for the Medication Delivery, BioScience and Renal segments, respectively, at December 31, 2003. The change in the goodwill balance during the quarter for each segment principally related to fluctuations in currency exchange rates.

Other intangible assets

The following is a summary of the company s intangible assets subject to amortization at March 31, 2004 and December 31, 2003. Intangible assets with indefinite useful lives are not material to the company.

(in millions, except amortization period data)	Developed technology, including patents	Manufacturing, distribution and other contracts	Other	Total
March 31, 2004				
Gross intangible assets	$814	$45	$77	$936
Accumulated amortization	298	19	21	338
Net intangible assets	$516	$26	$56	$598
Weighted-average amortization period (in years)	15	8	20	15
December 31, 2003				
Gross intangible assets	$802	$39	$74	$915
Accumulated amortization	279	14	18	311
Net intangible assets	$523	$25	$56	$604
Weighted-average amortization period (in years)	15	9	20	15

The amortization expense for these intangible assets was $16 million and $12 million for the three months ended March 31, 2004 and 2003, respectively. At March 31, 2004, the anticipated annual amortization expense for these intangible assets is $62 million, $57 million, $54 million, $47 million, $42 million and $41 million in 2004, 2005, 2006, 2007, 2008 and 2009, respectively.

Product warranties

The following is a summary of activity in the product warranty liability.

	As of and for the three months ended March 31,	
(in millions)	**2004**	**2003**
Beginning of period	$53	$53
New warranties and adjustments to existing warranties	3	8
Payments in cash or in kind	(6)	(8)
End of period	$50	$53

3. DISCONTINUED OPERATIONS

During the fourth quarter of 2002, the company recorded a $294 million pre-tax charge ($229 million on an after-tax basis) principally associated with management s decision to divest the majority of the services businesses included in the Renal segment. Refer to the 2003 Annual Report for further information.

During 2003, the company sold RMS Lifeline, Inc. and RMS Disease Management, Inc. and the Medication Delivery segment s offsite pharmacy admixture products and services business, and closed or had under contract the majority of transactions in connection with the divestiture of the Renal Therapy Services centers. Management expects the divestiture plan to be completed during 2004.

Net revenues relating to the discontinued businesses were $17 million and $48 million for the periods ended March 31, 2004 and 2003, respectively. The loss from the discontinued operations was $11 million for the three months ended March 31, 2004 (net of tax benefit of $4 million) and $1 million for the three months ended March 31, 2003 (net of tax benefit of $3 million).

Included in the pre-tax charge was $269 million pertaining to asset impairments, principally relating to goodwill and property and equipment. Also included in the charge was $25 million for cash costs, principally relating to severance and other employee-related costs associated with the elimination of approximately 75 positions, as well as legal and contractual commitment costs. The remaining reserve for cash costs of $8 million at March 31, 2004 is expected to be substantially utilized in 2004.

4. RESTRUCTURING INITIATIVES

Second quarter 2003 restructuring charge

During the second quarter of 2003, the company recorded a $337 million restructuring charge ($202 million, or $0.33 per diluted share, on an after-tax basis) principally associated with management s decision to close certain facilities and reduce headcount on a global basis. Management decided to take these actions in order to position the company more competitively and to enhance profitability. The company has closed 26 plasma collection centers across the United States, as well as a plasma fractionation facility located in Rochester, Michigan. In addition, the company is consolidating and integrating several facilities, including facilities in Maryland; Frankfurt, Germany; Issoire, France; and Mirandola, Italy. Management discontinued Baxter s recombinant hemoglobin protein program because it did not meet expected clinical milestones. Also included in the charge are costs related to other reductions in the company s workforce. As further discussed below, management is implementing additional restructuring initiatives during 2004.

Included in the 2003 pre-tax charge was $128 million for non-cash costs, principally to write down property, plant and equipment, and goodwill and other intangible assets due to impairment. Also included in the 2003 pre-tax charge was $209 million for cash costs, principally pertaining to severance and other employee-related costs associated with the elimination of approximately 3,200 positions worldwide.

The following summarizes the company s utilization of the reserve for cash costs during the first quarter of 2004.

(in millions)	Employee-related costs	Contractual and other costs	Total
Reserve at December 31, 2003	$ 97	$ 43	$140
Utilization	(25)	(12)	(37)
Reserve at March 31, 2004	$ 72	$ 31	$103

Approximately 87% of the targeted positions have been eliminated as of March 31, 2004. The majority of the costs are expected to be paid and the remaining positions are expected to be eliminated in 2004.

2004 restructuring initiatives

In January 2004, management announced plans (which were finalized during the second quarter of 2004) to implement additional actions to improve the company s financial position. These actions will include the elimination of approximately 3,500 to 4,000 additional positions, or approximately 7 to 8 percent of the global workforce. Nearly three quarters of the positions to be eliminated will impact general and administrative expenses. Baxter plans to reduce plasma production and close additional plasma collection centers. Management anticipates that a restructuring charge will be recorded in the second quarter of 2004, principally for severance and costs associated with the closing of facilities.

5. SECURITIZATIONS

Where economical, the company has entered into agreements with various financial institutions in which certain pools of receivables are sold. Refer to the 2003 Annual Report for further information regarding these arrangements. There have been no changes in the securitization arrangements, nor in the company s related accounting policies. The key assumptions used in measuring the fair values of the retained interests are substantially unchanged from that disclosed in the 2003 Annual Report.

The securitization arrangements resulted in net cash outflows of $43 million and $73 million for the three months ended March 31, 2004 and 2003, respectively. A summary of the activity is as follows.

	Three months ended March 31,	
(in millions)	**2004**	**2003**
Sold receivables at beginning of period	$ 742	$ 721
Proceeds from sales of receivables	375	460
Cash collections (remitted to the owners of the receivables)	(418)	(533)
Effect of currency exchange-rate changes	5	(8)
Sold receivables at end of period	$ 704	$ 640

6. PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS

Net pension and other postretirement benefits cost

The following is a summary of net expense relating to the company s pension and other postretirement benefit plans.

(in millions)	Three months ended March 31, 2004	2003
Pension benefits		
Service cost	$ 20	$ 16
Interest cost	39	33
Expected return on plan assets	(48)	(43)
Amortization of net loss, prior service cost and transition obligation	16	6
Net periodic pension benefit cost	$ 27	$ 12
Other benefits		
Service cost	$ 2	$ 2
Interest cost	8	7
Amortization of net loss and prior service cost	2	1
Net periodic other benefit cost	$ 12	$ 10

Medicare Prescription Drug, Improvement and Modernization Act

In December 2003, the Medicare Prescription Drug, Improvement and Modernization Act (the Act) was signed into law. The Act introduces a prescription drug benefit under Medicare (Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare (Part D). Detailed regulations necessary to implement the Act have not yet been issued. The effects of the Act are not recognized in the company s net expense and benefit obligation as management is not yet able to determine whether the company s benefits are actuarially equivalent to Medicare (Part D). However, based on preliminary analyses, management does not expect the Act to have a material impact on the company s consolidated financial statements.

7. LEGAL PROCEEDINGS, COMMITMENTS AND CONTINGENCIES

Refer to Part II - Item 1. Legal Proceedings below.

8. SEGMENT INFORMATION

The company operates in three segments, each of which are strategic businesses that are managed separately because each business develops, manufactures and sells distinct products and services. The segments and a description of their businesses are as follows: **Medication Delivery**, which provides a range of intravenous solutions and specialty products that are used in combination for fluid replenishment, general anesthesia, nutrition therapy, pain management, and antibiotic therapy; **BioScience**, which develops biopharmaceuticals, biosurgery products, vaccines and blood collection, processing and storage products and technologies for transfusion therapies; and **Renal**, which develops products and provides services to treat end-stage kidney disease.

Certain items are maintained at corporate headquarters (Corporate) and are not allocated to the segments. They primarily include most of the company s debt and cash and equivalents and related net interest expense, corporate headquarters costs, certain non-strategic investments and related income and expense, certain nonrecurring gains and losses, certain special charges (such as in-process research and development, restructuring and asset impairments), deferred income taxes, certain foreign currency fluctuations, the majority of foreign currency and interest rate hedging activities, and certain litigation liabilities and related insurance receivables.

Financial information for the company s segments for the quarter ended March 31 is as follows.

	Restated				
(in millions)	**Medication Delivery**	**BioScience**	**Renal**	**Other**	**Total**
Three months ended March 31,					
2004					
Net sales	$926	$810	$473	$	$2,209
Pre-tax income	151	122	80	(104)	249
2003					
Net sales	$848	$740	$407	$	$1,995
Pre-tax income	134	123	66	(40)	283

The following is a reconciliation of total segment amounts to totals per the condensed consolidated income statements.

	Restated	
	Three months ended March 31,	
(in millions)	**2004**	**2003**
Pre-tax income		
Total pre-tax income from segments	$353	$323
Unallocated amounts		
Interest expense, net	(21)	(19)
Certain currency exchange-rate fluctuations and hedging activities	(34)	(8)

Other Corporate items	(49)	(13)
Income from continuing operations before income taxes	$249	$283

9. SHARED INVESTMENT PLAN

As discussed in the 2003 Annual Report, in order to align management and shareholder interests, in 1999 the company sold 6.1 million shares of the company s stock to 142 of Baxter s senior managers for $198 million in cash. The participants used five-year full-recourse personal bank loans to purchase the stock at the May 3, 1999 closing price (adjusted for the company s stock split) of $31.81. Baxter has guaranteed repayment to the banks in the event a participant in the plan defaults on his or her obligations, which are due on May 6, 2004. The plan also includes certain risk-sharing provisions, which terminate on May 6, 2004. The company was entitled to 50% of any gain relating to stock sold on or before May 3, 2002. For stock sold after May 3, 2002 and through May 6, 2004, the company shares 50% in any loss incurred by the participants relating to a stock price decline (at the Baxter common stock closing price at March 31, 2004 of $30.89, the loss-sharing amount relating to shares held by participants on that date is approximately $2 million).

With respect to the guarantees, the company may take actions relating to participants and their assets to obtain full reimbursement for any amounts the company pays to the bank pursuant to the loan guarantee (in excess of any obligation under the risk-sharing provision). Baxter s maximum potential obligations for outstanding principal and interest and risk-sharing relating to this plan totaled $218 million as of March 31, 2004.

In May 2003, management announced that, in order to continue to align management and shareholder interests and to balance both the short- and long-term needs of Baxter, the board of directors authorized the company to provide a new three-year guarantee at the May 6, 2004 loan due date for the non-executive officer employees who remain in the plan, should they elect to extend their loans. As noted above, as of May 6, 2004, the 50% risk-sharing provision included in the current plan will terminate. The amount under the company s loan guarantee that will be effective on May 6, 2004 relating to the 73 eligible employees who have elected to extend their loans is $102 million.

No liability is recorded relating to the outstanding guarantees at March 31, 2004. The new three-year guarantee is not expected to have a material impact on the company s results of operations.

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

RESTATEMENTS OF PREVIOUSLY ISSUED CONSOLIDATED FINANCIAL STATEMENTS

Amendment No. 1

As discussed in Note 1A to the consolidated financial statements, the company has restated its previously issued financial statements for the years ended December 31, 2001, 2002 and 2003 and the first quarter of 2004. The restatement was primarily the result of the inappropriate application of accounting principles for revenue recognition and inadequate provisions for bad debts in Brazil during the period. Refer to Note 1A for further information, including the impact of the restatement for each of the restated periods included in this filing. As a result of the restatement, in aggregate, net sales decreased $37 million (0.2% of the originally reported amount) and net income decreased $33 million (1.5% of the originally reported amount) over the three-year period ended December 31, 2003. For the first quarter of 2004, net sales were unchanged as a result of the restatement and net income decreased $2 million (1.1% of the originally reported amount). For the first quarter of 2003, net sales decreased $2 million (0.1% of the originally reported amount) and net income decreased $2 million (0.9% of the originally reported amount).

Amendment No. 2

As discussed in Note 1B to the consolidated financial statements, the company has restated its previously issued financial statements for 2001 through 2003 and the first three quarters of 2004 as a result of inadequate reconciliations, leading to classification errors in tax and other related balance sheet accounts. Refer to Note 1B for further information, including the impact of the restatement for each of the restated periods included in this filing. As a result of the restatement, stockholders equity as of both March 31, 2004 and December 31, 2003 increased approximately $108 million, with offsetting decreases of approximately $157 to net tax liabilities and $49 million to goodwill. The restatement does not impact the consolidated statements of income or cash flows for the quarters ended March 31, 2004 and 2003.

Refer to the company s Form 10-K/A Amendment No. 2 for the year ended December 31, 2003 (which reflects the above-mentioned restatements) for management s discussion and analysis of financial condition and results of operations of the company for the year ended December 31, 2003. The following is management s discussion and analysis of the financial condition and results of operations of the company for the quarter ended March 31, 2004. The information in this discussion and analysis reflects the restatements, but is not otherwise updated.

RESULTS OF CONTINUING OPERATIONS

NET SALES

Restated	
Three months ended March 31,	Percent increase

(in millions)	2004	2003	
International	$1,190	$1,039	15%
United States	1,019	956	7%
Total net sales	$2,209	$1,995	11%

Currency exchange rate fluctuations benefited sales growth by 7 points during the three months ended March 31, 2004 principally because the United States Dollar weakened since the prior year quarter relative to the Euro. These fluctuations impacted sales growth for all three segments. Refer to Note 8 to the condensed consolidated financial statements for a summary of net sales by segment.

Medication Delivery

The Medication Delivery segment generated 9% sales growth during the three months ended March 31, 2004 (including 5 percentage points due to the favorable impact of foreign currency fluctuations), with the strongest sales growth in international markets. Increased sales of certain generic and branded pre-mixed drugs and drug delivery products contributed 2 points of sales growth. Sales of intravenous therapies, which principally include intravenous solutions and nutritional products, contributed 4 points to the segment s growth rate for the quarter. Sales of anesthesia and critical care products contributed 1 point to the growth rate, primarily due to increased sales of certain generic drugs. Sales of electronic infusion pumps and related tubing sets also contributed 1 point to the growth rate. Partially offsetting the growth in these product lines was the impact of management s 2003 decision to exit certain lower-margin distribution businesses outside the United States. The segment s sales growth in the United States during the first quarter of 2004 was not significantly impacted by the renegotiated long-term contracts with group purchasing organizations, principally Premier Purchasing Partners L.P. (Premier), the most significant of which became effective in February 2004. While sales growth during the remainder of 2004 is expected to be impacted by the reduced pricing included in these contracts, management believes that over time, the impact of reduced pricing will be substantially offset by increased sales volumes and product mix upgrades.

BioScience

Sales in the BioScience segment increased 9% for the three months ended March 31, 2004 (including 7 percentage points due to the favorable impact of foreign currency fluctuations), with sales growth strongest in the United States. The primary driver of the segment s growth rate for the quarter was increased sales of recombinants, contributing 6 points of growth. Recombinant growth was principally fueled by higher demand for Recombinate Antihemophilic Factor (rAHF) (Recombinate), as well as the launch of the advanced recombinant therapy, ADVATE (Antihemophilic Factor (Recombinant), Plasma/Albumin-Free Method) rAHF-PFM, which received regulatory approval in the United States in July 2003 and in Europe in March 2004. Of the 6 points of growth relating to recombinants, sales of ADVATE contributed 4 points, with an increased sales contribution expected during the remainder of 2004 as the launch of this new product continues and broadens in the United States and Europe. These factors were partially offset by the impact of the entry or re-entry into the marketplace in 2003 by certain competitors. Sales of plasma-based products, which were relatively flat for the quarter, were impacted by competitive pressures, as well as a continuing shift in the market from plasma-based to recombinant hemophilia products. As discussed further below, as a result of these competitive pressures, the company closed 26 plasma collection centers and a plasma fractionation plant during 2003, and plans to reduce plasma production and close additional centers during 2004, to improve the economics of the plasma business. Higher sales of anti-body therapies, including IVIG (immunoglobulin intravenous) for immune deficiencies, contributed 2 points to the growth rate for the quarter, and increased sales of biosurgery products contributed 1 point to the growth rate. Sales of transfusion therapies products contributed 1 point of growth, partially due to the continued launch and penetration of the ALYX platform, an automated blood collection system. Partially offsetting the growth in these product lines was the impact of lower sales of vaccines, principally due to lower sales of NeisVac-C for the prevention of meningitis C. Sales of vaccines are impacted by the timing of government tenders, and there were no significant tenders filled during the first quarter of 2004.

Renal

Sales from continuing operations in the Renal segment increased 16% for the three months ended March 31, 2004 (including 8 percentage points due to the favorable impact of foreign currency fluctuations), with sales growth strongest in international markets. Increased sales of products for peritoneal dialysis contributed 11 points to the segment s growth rate for the quarter. Increased penetration of products for peritoneal dialysis continues to be strongest in emerging markets such as Latin America and Asia, where many people with end-stage renal disease are currently under-treated. The majority of the remaining 5 points of growth during the three months ended March 31, 2004 was related to increased sales of hemodialysis products.

The following tables show key ratios of certain income statement items as a percent of sales.

GROSS MARGIN AND EXPENSE RATIOS

	Restated		
	Three months ended March 31,		
	2004	2003	Change
Gross margin	40.4%	44.0%	(3.6)pts
Marketing and administrative expenses	21.1%	20.8%	0.3pts

Foreign currency fluctuations, principally relating to the strengthened Euro, accounted for approximately 2 points of the gross margin decline from 2003 to 2004. Also, as discussed above, sales of the BioScience segment s plasma-based products have been impacted by increased competition and related pricing pressures, which, while stabilizing, unfavorably affected the gross margin for these products during the first quarter of 2004 as compared to the prior year quarter. In addition, costs associated with the company s employee pension and other postretirement benefit plans have increased since the prior year quarter (as further discussed below). These factors were partially offset by cost savings relating to the company s restructuring initiatives (as further discussed below).

Marketing and administrative expenses as a percent of sales increased slightly during the quarter primarily due to foreign currency fluctuations, increased employee pension and other postretirement benefit plan costs, and the impact of reduced costs in the prior year quarter due to a change in the employee vacation policy. These factors were partially offset by cost savings relating to the company s 2003 restructuring initiatives and other actions designed to reduce the company s expense base.

Expenses associated with the company s pension and other postretirement benefit plans increased $17 million during the first quarter of 2004, as detailed in Note 6, principally due to a reduction in the discount rate and the amortization of unrecognized losses. Refer to the 2003 Annual Report for further information.

RESEARCH AND DEVELOPMENT

	Three months ended March 31,		
(in millions)	**2004**	**2003**	**Percent increase**
Research and development (R&D) expenses	$ 136	$ 136	%
As a percent of sales	6.2%	6.8%	

R&D expenses in the first quarter of 2004 were flat as compared to the prior year. Management does not expect R&D spending to increase significantly for full year 2004, with increased spending on certain projects across the three segments offset by the benefits of the 2003 restructuring initiatives, and the termination of certain programs (such as the recombinant hemoglobin protein project, which was terminated in the second quarter of 2003).

RESTRUCTURING INITIATIVES

Second quarter 2003 restructuring charge

During the second quarter of 2003, the company recorded a $337 million restructuring charge ($202 million, or $0.33 per diluted share, on an after-tax basis) principally associated with management s decision to close certain facilities and reduce headcount on a global basis. Management decided to take these actions in order to position the company more competitively and to enhance the company s profitability. Refer to Note 4 for additional information.

During the first quarter of 2004, $37 million of the reserve for cash costs was utilized. Approximately 87% of the targeted positions have been eliminated as of March 31, 2004. The majority of the costs are expected to be paid and the majority of the remaining positions are expected to be eliminated by the end of 2004.

Management expects that the actions initiated in 2003 will generate incremental annual savings of approximately $0.15 to $0.20 per diluted share when fully implemented. The cost savings principally relate to employee compensation and primarily benefit the marketing and administrative expenses line in the consolidated income statement. Management estimates that the cost savings in the first quarter of 2004 were approximately $0.04 per diluted share, and expects that the full year 2004 savings will total approximately $0.15 per diluted share.

2004 restructuring initiatives

In January 2004, management announced plans (which were finalized during the second quarter of 2004) to implement additional actions to improve the company s financial position. These actions will include the elimination of approximately 3,500 to 4,000 additional positions, or approximately 7 to 8 percent of the global workforce. Nearly three quarters of the positions to be eliminated will impact general and administrative expenses. The company also intends to further enhance profitability and cash flows by adjusting its plasma production. Accordingly, Baxter plans to reduce plasma production and close additional plasma collection centers. Management anticipates that an after-tax restructuring charge of approximately $350 to $400 million, or $0.55 to $0.65 per diluted share, will be recorded in the second quarter of 2004, principally for severance and costs associated with the closing of facilities. Management anticipates that these additional initiatives will yield savings of $0.05 per diluted share in the second half of 2004, $0.20 to $0.25 per diluted share in 2005, and $0.30 to $0.35 per diluted share when fully implemented in 2006.

NET INTEREST EXPENSE

Net interest expense increased $2 million for the three months ended March 31, 2004 principally due to lower capitalized interest and higher effective interest rates.

OTHER EXPENSE, NET

Other expense decreased during the three months ended March 31, 2004. Included in other income and expense in both 2004 and 2003 were amounts relating to fluctuations in currency exchange rates, minority interests and income related to equity method investments. Other expense in 2003 included a $13 million pre-tax impairment charge relating to an investment in a publicly traded company, with the decline in value deemed to be other than temporary.

PRE-TAX INCOME

Refer to Note 8 to the condensed consolidated financial statements for a summary of financial results by segment. Certain items are maintained at the company s corporate headquarters and are not allocated to the segments. They primarily include certain foreign currency fluctuations, the majority of the foreign currency and interest rate hedging activities, net interest expense, income and expense related to certain non-strategic investments, corporate headquarters costs, certain nonrecurring gains and losses, and certain special charges (such as in-process research and development, restructuring and asset impairments). In addition, the above-mentioned increased costs associated with the pension and other postretirement benefit plans have not been completely allocated to the segments. The following is a summary of significant factors impacting the segments financial results.

Medication Delivery

Pre-tax income increased 13% for the three months ended March 31, 2004. The growth in pre-tax income was primarily the result of strong sales growth, the close management of costs, the benefits of the recent restructuring initiatives, and changes in currency exchange rates (as noted above, foreign currency hedging activities for all segments are recorded at corporate, and are not included in segment results). As noted above, while results for the first quarter of 2004 were not significantly impacted by the recently renegotiated long-term contracts with group purchasing organizations, principally Premier, sales and earnings growth during the remainder of 2004 is expected to be impacted by the reduced pricing included in these contracts.

BioScience

Pre-tax income decreased 1% (as restated) for the three months ended March 31, 2004. The decline in pre-tax income was primarily due to changes in currency exchange rates, lower sales of higher-margin vaccines, reduced gross margins for plasma-based products, and a modest increase in inventory reserves, partially offset by lower R&D spending as a result of the recent prioritization initiatives (including the termination of the recombinant hemoglobin protein project in 2003), the close management of costs, and the benefits of the recent restructuring initiatives.

Renal

Pre-tax income increased 21% (as restated) for the three months ended March 31, 2004. The increase in pre-tax income was primarily due to strong sales growth, changes in currency exchange rates, an improved sales mix, the close management of costs, and the benefits of the recent restructuring initiatives, partially offset by increased R&D spending.

INCOME TAXES

The effective income tax rate from continuing operations for the first quarter of 2004 and 2003 was 25% and 24%, respectively. The effective income tax rate was substantially unchanged, with minor differences principally due to changes in the mix of earnings between the various tax jurisdictions.

INCOME AND EARNINGS PER DILUTED SHARE FROM CONTINUING OPERATIONS

Income from continuing operations of $187 million (as restated), or $0.30 per diluted share (as restated), for the three months ended March 31, 2004 decreased 13% from the $215 million (as restated), or $0.36 per diluted share, reported in the prior year quarter. The significant factors causing the decline are discussed above.

LOSS FROM DISCONTINUED OPERATIONS

The loss from discontinued operations was $11 million and $1 million in the current and prior year quarter, respectively. Refer to Note 3 for further discussion of the discontinued operations. Management expects the divestiture plan will be completed during 2004.

CRITICAL ACCOUNTING POLICIES

The preparation of financial statements in accordance with generally accepted accounting principles (GAAP) requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. A summary of the company s significant accounting policies is included in Note 1 to the company s consolidated financial statements for the year ended December 31, 2003, which are included in the 2003 Annual Report. Certain of the company s

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accounting policies are considered critical, as these policies are the most important to the depiction of the company s financial statements and require significant, difficult or complex judgments by management, often employing the use of estimates about the effects of matters that are inherently uncertain. Such policies are summarized in the Management s Discussion and Analysis section of the 2003 Annual Report. There have been no significant changes in the application of the critical accounting policies since December 31, 2003.

LIQUIDITY AND CAPITAL RESOURCES

CASH FLOWS

Cash flows from continuing operations

The company reported cash outflows from continuing operations of $53 million (as restated) for the three months ended March 31, 2004. These cash outflows increased $31 million as compared to the prior year quarter. The increase in cash outflows was due to lower cash flows relating to accounts receivables and liabilities, payments related to the restructuring programs, and contributions to the pension trust, partially offset by higher earnings (before non-cash items) and improved cash flows relating to inventories.

Accounts Receivable

The decrease in cash flows relating to accounts receivable was partially due to reduced cash flows from the company s securitization arrangements, as detailed in Note 5. Management continues to increase its focus on working capital efficiency. With this increased focus, the company improved its accounts receivable collections (days sales outstanding improved from 62.8 days (as restated) at March 31, 2003 to 61.4 days (as restated) at March 31, 2004).

Inventories

The following is a summary of inventories at March 31, 2004 and December 31, 2003, as well as inventory turns for the first quarter of 2004 and 2003, by segment.

	Restated			
	Inventories		**Inventory turns for the three months ended March 31,**	
(in millions, except inventory turn data)	**March 31, 2004**	**December 31, 2003**	**2004**	**2003**
BioScience	$1,369	$1,378	1.42	1.37

Medication Delivery	590	528	3.62	3.69
Renal	209	198	4.00	3.51
Total	$2,168	$2,104	2.34	2.27

Inventory balances increased $64 million (as restated) from December 31, 2003 to March 31, 2004. A portion of the increase related to fluctuations in currency exchange rates (particularly the strengthened Euro), which did not impact cash flows. Inventory turns are impacted by seasonality in certain of the company s businesses, and are generally highest in the fourth quarter of the year, and lower earlier in the year, for these businesses.

Liabilities, Including Restructuring Payments and Contributions to the Pension Trust

Cash flows relating to accounts payable and accrued liabilities were lower in the first quarter of 2004 as compared to the prior year quarter, partially due to the timing of payments relating to income taxes. Cash payments associated with restructuring programs increased $30 million in the first quarter of 2004. The company also contributed $54 million to its pension trust during the first three months of 2004, versus no contributions in the prior year quarter.

Cash flows from discontinued operations

Cash outflows relating to discontinued operations decreased $5 million during the first quarter, from a $6 million outflow in 2003 to a $1 million outflow in 2004. As discussed in Note 3 and above, the company has divested the majority of the discontinued operations and plans to complete the divestiture plan in 2004.

Cash flows from investing activities

Capital Expenditures

Capital expenditures decreased for the three months ended March 31, 2004 by $85 million, from $175 million (as restated) in 2003 to $90 million (as restated) in 2004. As discussed in the 2003 Annual Report, management is reducing its level of investments in capital expenditures in 2004 as certain significant long-term projects are completed. Management currently anticipates that the company s capital expenditures will not exceed $650 million in 2004. Construction in progress also decreased 8% from December 31, 2003 to March 31, 2004, as the company placed assets into service.

Acquisitions and Investments In and Advances to Affiliates

Net cash outflows relating to acquisitions and investments in and advances to affiliates decreased by $57 million during the first three months of 2004, from $71 million in 2003 to $14 million in 2004. The current quarter included outflows relating to the 2003 acquisition of certain assets of Alpha Therapeutic Corporation, which are included in the BioScience segment. The 2003 outflows included the funding of a $50 million loan to

Cerus Corporation, a minority investment holding which is included in the BioScience segment. Also included in net cash outflows in 2003 was an $11 million common stock investment in Acambis, Inc., which was divested later in 2003.

Divestitures and Other

Net cash flows relating to divestitures and other totaled $26 million in 2004, and principally related to the sale of a building and the return of collateral.

Cash flows from financing activities

Debt Issuances, Net of Redemptions and Other Payments of Debt

Debt issuances, net of redemptions and other payments of debt, decreased $827 million in the first quarter, from $1.018 billion in 2003 to $191 million in 2004. As discussed in the 2003 Annual Report, in March 2003 the company issued $600 million of term debt in anticipation of the redemption of approximately $800 million of convertible debentures in May 2003, when the holders exercised their rights to put the debentures to the company.

Other Financing Activities

Common stock cash dividends increased in 2004 by $15 million due to a higher level of common shares outstanding. Cash received for stock issued under employee benefit plans increased by $15 million principally due to a higher level of stock option exercises and purchases under the company s employee stock purchase plans. Stock repurchases decreased from 2003 to 2004. In the first quarter of 2004 the company paid $11 million to repurchase stock from Shared Investment Plan (SIP) participants. Refer to Note 9 and Part II, Item 2(e), Changes In Securities, Use of Proceeds and Issuer Purchases of Equity Securities, of this report for further information regarding the SIP and these repurchases. In the first quarter of 2003 the company purchased 3.1 million shares of common stock for $153 million from counterparty financial institutions in conjunction with the settlement of equity forward agreements. Refer to the 2003 Annual Report for further information.

CREDIT FACILITIES, ACCESS TO CAPITAL, AND COMMITMENTS AND CONTINGENCIES

Refer to the 2003 Annual Report for further discussion of the company s credit facilities, access to capital, and commitments and contingencies.

The company had $646 million (as restated) of cash and equivalents at March 31, 2004. The company also maintains two revolving credit facilities, which totaled $1.4 billion at March 31, 2004, and which have funding expiration dates through November 2007. The facilities enable the company to borrow funds on an unsecured basis at variable interest rates. The company has never drawn on these facilities and does not intend to do so in the foreseeable future. Management believes these credit facilities are adequate to support ongoing operational requirements. The credit facilities contain certain covenants, including a maximum net-debt-to-capital ratio and a minimum interest coverage ratio. At March 31, 2004, as in prior periods, the company was in compliance with all covenants. The company s net-debt-to-capital ratio, as defined below, of 42.4% (as restated) at March 31, 2004 was well below the credit facilities net-debt-to-capital covenant. Similarly, the company s actual interest coverage ratio of 10.4 to 1 (as restated) in the first quarter of 2004 was well in excess of the minimum interest coverage ratio covenant. The net-debt-to-capital ratio, which is calculated in accordance with the company s primary credit agreements, and is not a measure defined by GAAP, is calculated as net debt (short-term and long-term debt and lease obligations, less cash and equivalents) divided by capital (the total of net debt and stockholders equity). The net-debt-to-capital ratio at March 31, 2004 and the corresponding covenant in the company s credit agreements give 70% equity credit to the company s equity units. Refer to the 2003 Annual Report for a description of the equity units, which were issued in December 2002. The minimum interest coverage ratio is a four-quarter rolling calculation of the total of income from continuing operations before income taxes plus interest expense (before interest income), divided by interest expense (before interest income). Baxter also maintains certain other short-term credit arrangements. The above-mentioned financial statement restatement had no impact on the company s compliance with the financial covenants in its debt agreements.

The company intends to fund its short-term and long-term obligations as they mature through cash on hand, future cash flows from operations, by issuing additional debt, or by issuing common stock. As of March 31, 2004, the company can issue up to $399 million of securities, including

debt, common stock and other securities, under an effective registration statement filed with the Securities and Exchange Commission. The company s debt ratings at March 31, 2004 were A3 by Moody s, A- by Standard & Poor s and A- by Fitch on senior debt, and P2 by Moody s, A2 by Standard & Poor s and F2 by Fitch on short-term debt (all with negative outlooks, with Moody s ratings under review for possible downgrade based on concerns regarding the transition to new senior management, challenges in certain businesses, and other factors). The first quarter 2004 downgrade and any future downgrades of Baxter s credit ratings unfavorably impact the financing costs associated with the company s credit arrangements and future debt issuances. Certain specified downgrades, if they occur in the future, would also require the company to post additional collateral pursuant to certain of its arrangements. However, any future downgrades would not affect the company s ability to draw on its credit facilities, and would not result in an acceleration of the scheduled maturities of any of the company s outstanding debt.

The company s ability to generate cash flows from operations, issue debt, enter into other financing arrangements and attract long-term capital on acceptable terms could be adversely affected in the event there is a material decline in the demand for the company s products, deterioration in the company s key financial ratios or credit ratings, or other significantly unfavorable changes in conditions. Management believes it has sufficient financial flexibility in the future to issue debt, enter into other financing arrangements, and attract long-term capital on acceptable terms as may be needed to support the company s growth objectives.

See Part II - Item 1. Legal Proceedings for a discussion of the company s legal contingencies. Upon resolution of any of these uncertainties, the company may incur charges in excess of presently established reserves. While such a future charge could have a material adverse impact on the company s net income or cash flows in the period in which it is recorded or paid, based on the advice of counsel, management believes that any outcome of these actions, individually or in the aggregate, will not have a material adverse effect on the company s consolidated financial position.

FORWARD-LOOKING INFORMATION

The matters discussed in this report that are not historical facts include forward-looking statements. These statements are based on the company s current expectations and involve numerous risks and uncertainties. Some of these risks and uncertainties are factors that affect all international businesses, while some are specific to the company and the health-care arenas in which it operates. Many factors could affect the company s actual results, causing results to differ, and possibly differ materially, from those expressed in any such forward-looking statements. These factors include, but are not limited to:

- the company s ability to realize in a timely manner the anticipated benefits of restructuring initiatives;
- the effect of economic conditions;
- the impact of geographic and/or product mix on the company s sales;
- actions of regulatory bodies and other government authorities, including the FDA and foreign counterparts that could delay, limit or suspend product sales and distribution;
- product quality and/or patient safety concerns, leading to product recalls, withdrawals, launch delays or declining sales;
- product development risks;

interest rates;

technological advances in the medical field;

demand for and market acceptance risks for new and existing products, such as ADVATE (Antihemophilic Factor (Recombinant), Plasma/Albumin-Free Method) rAHF-PFM, and other technologies;

the impact of competitive products and pricing, including generic competition, drug reimportation and disruptive technologies;

inventory reductions or fluctuations in buying patterns by wholesalers or distributors;

foreign currency exchange rates;

the availability of acceptable raw materials and component supply;

global regulatory, trade and tax policies;

regulatory, legal or other developments relating to the company s A, AF and AX series dialyzers;

- the ability to obtain adequate insurance coverage at reasonable cost;
- the ability to enforce patents;
- patents of third parties preventing or restricting the company s manufacture, sale or use of affected products or technology;
- reimbursement policies of government agencies and private payers;
- internal and external factors that could impact commercialization;
- results of product testing; and
- other factors described elsewhere in this report or in the company s other filings with the Securities and Exchange Commission.

Additionally, as discussed in Part II Item 1. Legal Proceedings, upon the resolution of certain legal matters, the company may incur charges in excess of presently established reserves. Any such charge could have a material adverse effect on the company s results of operations or cash flows in the period in which it is recorded.

Currency fluctuations are also a significant variable for global companies, especially fluctuations in local currencies where hedging opportunities are not economic or not available. If the United States Dollar strengthens significantly against foreign currencies, the company s ability to realize projected growth rates in its sales and net earnings outside the United States, as reported in United States Dollars, could be negatively impacted.

Management believes that its expectations with respect to forward-looking statements are based upon reasonable assumptions within the bounds of its knowledge of the company s business and operations, but there can be no assurance that the actual results or performance of the company will conform to any future results or performance expressed or implied by such forward-looking statements. The company does not undertake any obligation to update any forward-looking statements as a result of new information, future events, changed assumptions or otherwise, and all forward-looking statements speak only as of the time when made.

Item 4. Controls and Procedures

Controls and Procedures. The company carried out an evaluation, under the supervision and with the participation of the company s Disclosure Committee and the company s management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the company s disclosure controls and procedures (as such term is defined in Rules 13a-15(d) or 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of the end of the quarterly period covered by this report. The company s disclosure controls and procedures are designed to ensure that information required to be disclosed by the company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported on a timely basis and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the company s disclosure controls and procedures were not effective as of March 31, 2004 for the reasons described below.

The company has restated its previously issued financial results for the years 2001 through 2003, and the first three quarters of 2004. This restatement was primarily the result of a material weakness that existed as it relates to the controls surrounding the income tax accounts. Specifically, current income taxes payable were not reconciled to expected tax payments due, and the company did not adequately review the difference between the income tax basis and financial reporting basis of assets and liabilities and reconcile the difference to recorded deferred income tax assets and liabilities. Refer to Note 1B to the consolidated financial statements for further information regarding this restatement. To address this material weakness, subsequent to December 31, 2004, the company s management has taken the following actions:

1. Performed an extensive study and reconciliation of the income tax accounts.

2. During that study, the company identified adjustments to the income tax accounts that relate to prior periods.

3. Assessed the materiality of these adjustments with the Chief Executive Officer and the Chief Financial Officer and the Audit Committee and concluded that the historical consolidated financial statements indicated above should be restated.

As a result of these actions, management believes that the financial statements included in this report fairly present in all material respects the company s financial condition, results of operations and cash flows for the periods presented. In addition, the more enhanced reconciliation procedures performed to address this issue subsequent to the 2004 year-end will continue to be performed in the future to ensure this matter is remediated.

In addition, as previously disclosed in the company s Amendment to its Quarterly Report on Form 10-Q for the quarter ended March 31, 2004, in August 2004 the company restated its previously issued financial results for the years 2001 through 2003, and for the first quarter of 2004. This restatement was primarily the result of the inappropriate application of accounting principles for revenue recognition and inadequate provisions for bad debts in Brazil during this period. Senior management became aware of these issues in 2004 through the reporting procedures established under Baxter s Global Business Practice Standards. Upon becoming aware of the issues in Brazil, senior management, with the assistance of the company s internal audit team, conducted a preliminary investigation. This preliminary investigation was followed by a more comprehensive investigation by the Audit Committee of Baxter s Board of Directors, with the assistance of independent legal counsel and forensic and other accountants. Refer to Note 1A to the consolidated financial statements for further information regarding this restatement.

The investigations described above identified the following, which collectively constitute a material weakness in the company s internal control over financial reporting:

- an ineffective control environment maintained by senior management in Brazil, including intentional overrides by senior management in Brazil of internal controls;
- inadequate revenue recognition controls in Brazil;
- inadequate controls in Brazil to ensure adherence to generally accepted accounting principles for loss contingencies, including bad debts; and
- ineffective financial review by management responsible for the Intercontinental region, which includes Latin America.

During the third and fourth quarters of 2004, the company took several actions that it believes has remediated this material weakness. These actions include:

- Terminated four members of senior management in the company s Brazilian operations and replaced the Vice President, Finance responsible for the Intercontinental region;
- Completed monthly detailed internal audits of the Brazilian operations, beginning in July 2004, with an emphasis on the areas that gave rise to the inaccurate financial reporting;
- Completed additional training for finance, accounting and sales personnel in Brazil on appropriate accounting for revenue recognition;
- Completed additional training for finance and accounting personnel in Brazil on accounting and reporting policies, including those relating to accounting in accordance with Statement of Financial Accounting Standards No. 5 Accounting for Contingencies and SEC Staff Accounting Bulletin No. 99 Materiality;
- Completed enhanced training for employees in Brazil regarding Baxter s Global Business Practice Standards, including obligations to maintain accurate books and records and to report wrongdoing promptly;
- Implemented enhanced financial review procedures at the Intercontinental region level, including quarterly financial reviews for each significant country;
- Hired a director of internal control for the Intercontinental region;
- Implemented improved procedures for reporting legal contingencies and establishing appropriate legal reserves, and provided training on these procedures;
- Engaged a prominent independent public accounting firm (other than PricewaterhouseCoopers LLP) to perform a comprehensive review of internal control over financial reporting in Brazil;
- Implemented new controls in Brazil relating to the recording of revenues and loss contingencies, including new revenue recognition procedures with enhanced documentation requirements, monitoring of inventory levels at distributors and specific tracking of equipment installation; and

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Implemented new procedures in Brazil for determining bad debt reserve requirements.

The changes to internal control over financial reporting described above were implemented subsequent to the quarter ended March 31, 2004. There has been no change in the company s internal control over financial reporting that occurred during the quarter ended March 31, 2004 that has materially affected, or is reasonably likely to materially affect, the company s internal control over financial reporting.

Review by Independent Registered Public Accounting Firm

Reviews of the interim condensed consolidated financial information included in this Quarterly Report on Form 10-Q/A Amendment No. 2 for the three months ended March 31, 2004 and 2003 have been performed by PricewaterhouseCoopers LLP, the company s independent registered public accounting firm. Their report on the interim condensed consolidated financial information follows. This report is not considered a report within the meaning of Sections 7 and 11 of the Securities Act of 1933 and therefore, the independent accountants liability under Section 11 does not extend to it.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of

Baxter International Inc.:

We have reviewed the accompanying condensed consolidated balance sheet of Baxter International Inc. and its subsidiaries as of March 31, 2004, and the related condensed consolidated statements of income for each of the three-month periods ended March 31, 2004 and 2003 and the condensed consolidated statements of cash flows for the three-month periods ended March 31, 2004 and 2003. These interim financial statements are the responsibility of the Company s management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We previously audited in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2003, and the related consolidated statements of income, cash flows and stockholders equity and comprehensive income for the year then ended (not presented herein), and in our report dated February 20, 2004, except for Note 1A which is as of August 9, 2004 and Note 1B which is as of March 14, 2005, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2003, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

As described in Notes 1A and 1B, the Company has restated its previously issued consolidated financial statements.

/s/ PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chicago, Illinois
May 6, 2004, except for Note 1A which is as of August 9, 2004 and Note 1B which is as of March 28, 2005

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.

BAXTER INTERNATIONAL INC.
(Registrant)

Date: March 31, 2005

By: /s/ John J. Greisch

John J. Greisch
Corporate Vice President and Chief Financial Officer

EXHIBITS FILED WITH SECURITIES AND EXCHANGE COMMISSION

Number	Description of Exhibit
10.23*	Long-Term Incentive Plan, as amended and restated effective February 24, 2004, filed as exhibit 10.23 to the company s quarterly report on Form 10-Q for the quarter ended March 31, 2004
10.35*	Employment Agreement between Robert L. Parkinson, Jr. and Baxter International Inc. dated April 19, 2004, filed as exhibit 10.35 to the company s quarterly report on Form 10-Q for the quarter ended March 31, 2004
15	Letter Re Unaudited Interim Financial Information.
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes - Oxley Act of 2002
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes - Oxley Act of 2002
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. 1350
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. 1350

* Incorporated herein by reference.