# GALAPAGOS

Limited Liability Company
Generaal De Wittelaan L11 A3, 2800 Mechelen, Belgium
Company number: 0466.460.429
RLE Antwerp, division Mechelen

(the "**Company**")

# Special report of the Board of Directors in accordance with Article 596 and 598 of the Belgian Companies Code

**Cancellation of the preferential subscription rights of the existing shareholders in favor of Gilead Biopharmaceutics Ireland Unlimited Company in the framework of the proposed capital increase under the authorized capital**

## 1 Introduction

The Company controls certain intellectual property rights with respect to the compound known as filgotinib.

On 16 December 2015, the Company entered into a license and collaboration agreement with Gilead Biopharmaceutics Ireland Unlimited Company (hereinafter "**Gilead**"), granting Gilead a license under the intellectual property rights with respect to filgotinib with a view to co-developing and co-promoting products comprising filgotinib on the terms and conditions as determined in such agreement (hereinafter the "**License and Collaboration Agreement**").

As part of the collaboration between the Company and Gilead, the latter committed to invest an aggregate cash amount of up to USD 425,000,000 (hereinafter the "**Investment Amount**") in the share capital of the Company through a private placement of shares. Thereto the Company intends to increase its share capital with an aggregate amount of up to the Euro equivalent of the Investment Amount (share capital and share premium) (hereinafter the "**Capital Increase**"), within the framework of the authorized capital and with the cancellation of the preferential subscription rights of the existing shareholders for the benefit of Gilead. The terms and conditions of the equity investment by Gilead have been agreed upon with the Company by entering into a subscription agreement on 16 December 2015 (simultaneously with the License and Collaboration Agreement) (hereinafter the "**Subscription Agreement**").

This special report is established on 19 January 2016 by the board of directors of the Company pursuant to articles 596 and 598 of the Belgian Companies Code.

This special report has been drawn up in order to account for the Capital Increase within the framework of the authorized capital and to justify the cancellation of the preferential subscription rights of the existing shareholders for the benefit of Gilead.

## 2 Proposed Capital Increase

### 2.1 Purpose of the Capital Increase

Phase 2 trial data show that filgotinib has the potential to be an effective and well-tolerated oral therapy for patients with rheumatoid arthritis (DARWIN studies) and Crohn's disease (FITZROY study). The phase 3 trials in rheumatoid arthritis and Crohn's disease will start in 2016 pending the successful outcome of discussions with regulatory authorities.

The board of directors is of the opinion that the collaboration and strategic partnership with Gilead, of which this investment forms an integral part, will allow the Company to pursue its goal of rapidly delivering therapies to patients. Therefore, this cooperation is of a strategic importance for the future growth and development of the Company. The newly injected capital resulting from the Capital Increase shall significantly strengthen the cash position of the Company and can be used for the co-development and co-promotion of filgotinib and further research and development activities exploring possible other indications and new compounds.

Finally, as a result of the collaboration with, and investment by, Gilead, the Company enters into the next phase of its evolution and further strengthens its position as a leading European clinical-stage biotechnology company.

## 2.2 Structure of the Capital Increase

The board of directors wishes to increase the capital within the framework of the authorized capital and with the cancellation of the preferential subscription rights of the existing shareholders for the benefit of Gilead.

### 2.2.1 Authorized capital

(a) Historic Use

On 23 May 2011, the Company's extraordinary shareholders' meeting has resolved to renew the authorization to the board of directors with respect to the use of the authorized capital. By this renewed authorization, the board was authorized to increase the share capital in one or more times with an amount of EUR 142,590,770.44. This authorization is split in two tranches. The authorization with respect to the first tranche of 25% (EUR 35,647,692.61) of the authorized capital can be used by the board of directors by normal resolution. The authorization with respect to the second tranche of 75% (EUR 106,943,077.83) of the authorized capital can only be used upon unanimous resolution of the board of directors in which all directors are present or represented. Furthermore, this second tranche can only be used in the context of the following purposes:

(i) the entire or partial financing of a transaction through the issue of new shares of the Company, whereby "transaction" is defined as a merger or acquisition (in shares or cash), a corporate partnership, and an in-licensing deal,

(ii) the issue of warrants in the framework of the remuneration policy for employees, directors and independent consultants of the Company and its subsidiaries, and

(iii) the defense of the Company against a hostile take-over bid, and

(iv) strengthening of the cash position of the Company.

The renewed authorization to use the authorized capital is valid for a period of five years as from 23 May 2011. The board of directors may, in the context of the authorized capital, issue shares with or without voting rights. The board may also issue convertible bonds or warrants. The board may issue shares as consideration for contributions in cash or in kind, with or without a share premium. If the board asks a share premium, such premium shall be booked on a non-available reserve account. Such account can only be reduced or transferred after a decision of an extraordinary shareholders' meeting of the Company adopted in the manner required for amending the articles of association.

The board may, within the authorized capital, limit or cancel the preferential subscription rights of the existing shareholders but only in the interest of the

Company. Furthermore, the board has the authority to cancel the preferential subscription rights of the existing shareholders for the benefit of certain persons, other than employees of the Company or its subsidiaries.

The board of directors is also authorized to amend the articles of association of the Company in accordance with the capital increase that has been effectuated in the framework of the authorized capital.

On 3 September 2012 the board of directors partially used its renewed authorization for the use of the authorized capital a first time, with cancellation of the preferential subscription rights, for the issuance of the Warrant Plan 2012, which, after final establishment of the acceptances, relates to maximum 481,140 new shares to be issued. The new shares to be issued under the Warrant Plan 2012 will only be booked as capital to the amount of the fractional value, whereby fractional value means the fractional value of the existing shares on the date of the issuance of the warrants. The difference between the fractional value and the issuance price will be booked as share premium. By the issuance of the Warrant Plan 2012 the board used EUR 2,602,967.40 of the authorized capital, as indeed said warrants can result in the issuance of maximum 481,140 new shares, to be multiplied with the then current fractional value of (rounded up) EUR 5.41 per share.

On 29 April 2013 the board of directors partially used its renewed authorization for the use of the authorized capital a second time, with cancellation of the preferential subscription rights, for a private placement of 2,696,831 new shares at EUR 20.00 per share, resulting in an increase of the share capital with EUR 14,589,855.71 (plus share premium of EUR 39,346,764.29).

On 16 May 2013 the board of directors partially used its renewed authorization for the use of the authorized capital a third time, with cancellation of the preferential subscription rights, for the issuance of the Warrant Plan 2013, which, after final establishment of the acceptances, relates to maximum 602,790 new shares to be issued. The new shares to be issued under the Warrant Plan 2013 will only be booked as capital to the amount of the fractional value, whereby fractional value means the fractional value of the existing shares on the date of the issuance of the warrants. The difference between the fractional value and the issuance price will be booked as share premium. By the issuance of the Warrant Plan 2013 the board used EUR 3,261,093.90 of the authorized capital, as indeed said warrants can result in the issuance of maximum 602,790 new shares, to be multiplied with the then current fractional value of (rounded up) EUR 5.41 per share.

On 18 September 2013 the board of directors partially used its renewed authorization for the use of the authorized capital a fourth time, with cancellation of the preferential subscription rights, for the issuance of the Warrant Plan 2013 (B), which, after final establishment of the acceptances, relates to maximum 75,000 new shares to be issued. The new shares to be issued under the Warrant Plan 2013 (B) will only be booked as capital to the amount of the fractional value, whereby fractional value means the fractional value of the existing shares on the date of the issuance of the warrants. The difference between the fractional value and the issuance price will be booked as share premium. By the issuance of the Warrant Plan 2013 (B) the board used EUR 405,750 of the authorized capital, as indeed said warrants can result in the issuance of maximum 75,000 new shares, to be multiplied with the then current fractional value of (rounded up) EUR 5.41 per share.

On 25 July 2014 the board of directors partially used its renewed authorization for the use of the authorized capital a fifth time, with cancellation of the preferential subscription rights, for the issuance of the Warrant Plan 2014, which, after final establishment of the acceptances, relates to maximum 571,660 new shares to be issued. The new shares to be issued under the Warrant Plan 2014 will only be booked as capital to the amount of the fractional value, whereby fractional value means the fractional value of the existing shares on the date of the issuance of the warrants. The difference between the fractional value and the issuance price will be booked as share premium. By the issuance of the Warrant Plan 2014 the board used EUR 3,092,680.60 of the authorized capital, as indeed said warrants can result in the issuance of maximum 571,660 new shares, to be multiplied with the then current fractional value of (rounded up) EUR 5.41 per share.

On 15 October 2014 the board of directors partially used its renewed authorization for the use of the authorized capital a sixth time, with cancellation of the preferential subscription rights, for the issuance of the Warrant Plan 2014 (B), which, after final establishment of the acceptances, relates to maximum 150,000 new shares to be issued. The new shares to be issued under the Warrant Plan 2014 (B) will only be booked as capital to the amount of the fractional value, whereby fractional value means the fractional value of the existing shares on the date of the issuance of the warrants. The difference between the fractional value and the issuance price will be booked as share premium. By the issuance of the Warrant Plan 2014 (B) the board used EUR 811,500 of the authorized capital, as indeed said warrants can result in the issuance of maximum 150,000 new shares, to be multiplied with the then current fractional value of (rounded up) EUR 5.41 per share.

On 30 April 2015 the board of directors partially used its renewed authorization for the use of the authorized capital a seventh time, with cancellation of the preferential subscription rights, for the issuance of the Warrant Plan 2015, which, after final establishment of the acceptances, relates to maximum 532,053 new shares to be issued. The new shares to be issued under the Warrant Plan 2015 will only be booked as capital to the amount of the fractional value, whereby fractional value means the fractional value of the existing shares on the date of the issuance of the warrants. The difference between the fractional value and the issuance price will be booked as share premium. By the issuance of the Warrant Plan 2015 the board used EUR 2,878,406.73 of the authorized capital, as indeed said warrants can result in the issuance of maximum 532,053 new shares, to be multiplied with the then current fractional value of (rounded up) EUR 5.41 per share.

On 19 May 2015, the board of directors used its renewed authorization for the use of the authorized capital an eighth time, with cancellation of the preferential subscription rights, to increase our share capital by EUR 40,750,819.59 (plus EUR 237,951,643.41 in share premium) by means of a public offering in the United States of 5,746,000 shares in the form of American Depositary Shares at a price of USD 42.05 per ADS, before underwriting discounts, and a private placement in Europe and countries outside of the United States and Canada of 1,786,499 shares at price of EUR 37.00 per share, before underwriting discounts.

On 21 December 2015, the board of directors used its renewed authorization for the use of the authorized capital a ninth time, with cancellation of the preferential subscription rights for the issuance of the Warrant Plan 2015 RMV and Warrant Plan 2015 (B), which, subject to acceptance of the offered warrants by the plans' beneficiaries, relates to maximum 700,000 new shares to be issued. The new shares to be issued under the Warrant Plan 2015 RMV and Warrant Plan 2015 (B) will only be booked as capital to the amount of the fractional value, whereby fractional value means the fractional value of the existing shares on the date of the issuance of the warrants. The difference between the fractional value and the issuance price will be booked as share premium. By the issuance of the Warrant Plan 2015 RMV and Warrant Plan 2015 (B) the board used a maximum of EUR 3,787,000 of the authorized capital, as indeed said warrants can result in the issuance of maximum 700,000 new shares, to be multiplied with the then current fractional value of (rounded up) EUR 5.41 per share.

(b) Authorized Capital - Availability

On the date of this report, an aggregate amount of EUR 68,393,073.93 of the authorized capital has been used, as a result of which EUR 74,197,696.51 of the authorized capital is still available.

Under the hypothesis of a full and irrevocable adoption and acceptance of the aforementioned 700,000 warrants under the Warrant Plan 2015 (B) and Warrant Plan 2015 RMV, an aggregate amount of EUR 72,180,073.93 of the authorized capital would be used, as a result of which EUR 70,410,696.51 of the authorized capital would still be available.

The contemplated Capital Increase, as further described under this Section 2.2, by the proposed decision of the board to issue 6,760,701 new shares in the framework of the Subscription Agreement with Gilead, is therefore still within the limits of the total authorization of the authorized capital (and more specifically, the second tranche of 75% of the total authorization), taking into account the current accounting par value of (rounded up) EUR 5.41 per share as it would result in an increase of the share capital by EUR 36,575,392.41 (plus a share premium of EUR 355,545,265.59).

### 2.2.2 Subscription Amount

Within the framework of the authorized capital the board of directors wishes to utilize its authorization and to increase the capital of the Company with EUR 392,120,658, which amount is obtained by performing the following actions in the following order: (a) dividing the Investment Amount of USD 425,000,000 by the agreed-upon exchange rate of 1.08385; (b) dividing this amount by the agreed-upon issue price of the new shares of EUR 58.00; (c) rounding the latter amount down to the nearest whole number; and (d) by multiplying the resulting amount with the agreed upon issue price of the new shares of EUR 58.00 (the "**Subscription Amount**").

As set out in Section 2.2.1 of this Report, the Company's authorized capital allows the Company to increase its capital (including share premiums) with the Subscription Amount.

### 2.2.3 Issue Price

In the Subscription Agreement, the issue price for the new shares has been determined at EUR 58.00 per share, which represents a 20% premium as compared to the average of the closing prices of the Company's shares on Euronext during the thirty calendar days preceding the date of signing the Subscription Agreement, thus complying with article 598 of the Belgian Companies Code (the "**Issue Price**").

The portion of the Issue Price per new share up to the accounting par value of (rounded up) EUR 5.41, will be recorded on the "capital" account, i.e. an aggregate amount of EUR 36,575,392.41. The balance of the issue price per share, i.e. an aggregate amount of EUR 355,545,265.59, will be recorded on a non-available reserve account that can only be reduced or transferred by a decision of the shareholders' meeting adopted in the manner required for amending the articles of association.

#### 2.2.4 The new shares

The board of directors proposes that the Company will be issuing 6,760,701 new shares to Gilead following the Capital Increase, i.e. the Subscription Amount divided by the Issue Price.

The new shares will not have a nominal value and will each represent the same fraction of the capital as the other outstanding shares of the Company.

The new shares will carry the same rights as all outstanding shares and will equally share in the results of the Company.

#### 2.2.5 Listing and tradability of the new shares

The listing and trading of the new shares on Euronext (Brussels and Amsterdam) will be requested following the issuance of such new shares and the effective listing will be subject to regulatory approval of a listing prospectus.

## 3 Consequences for the Company's existing shareholders

The dilution and effect on the equity value of the Company that will result from the Capital Increase (including share premium) are indicatively set out in the tables below.

The tables below are based on the existing situation that the Company has a registered capital on the date of this report of EUR 211,388,857.22, represented by 39,076,342 shares. The accounting par value of the shares amounts to (rounded up) EUR 5.41.

The tables below do not take into account the exercise of any outstanding warrants under the warrant plans of the Company and the dilutive effect thereof. The exercise of all granted warrants that are still outstanding under the existing plans can possibly lead to the creation of up to 2,805,692 additional shares. This excludes the up to 700,000 warrants created subject to acceptance under Warrant Plan 2015 (B) and Warrant Plan 2015 RMV which, if accepted in full, could lead to the creation of up to 700,000 additional shares.

### 3.1 Dilution resulting from the Capital Increase based on the current number of shares

The table below shows the dilution of voting power and liquidation and dividend rights that will result from the Capital Increase.

| Current number of shares | Number of shares to be issued as a result of the Capital Increase | Dilution of existing shareholders |
|---|---|---|
| 39,076,342 | 6,760,701 | 14.75% |

### 3.2 Effect of the Capital Increase on the equity of the Company

Following the Capital Increase, the equity of the Company shall increase for an amount equal to the Subscription Amount. As the Issue Price is higher than the equity value per share before the Capital Increase, there is a positive effect on the equity value per share for the existing shareholders as set out in the tables below.

Existing situation before the Capital Increase

| | |
|---|---|
| Number of shares before the Capital Increase | 39,076,342 |
| Equity of the Company[1] | EUR 419,381,349 |
| Equity value per share before the Capital Increase | EUR 10.73 |

Effect of the Capital Increase

| | |
|---|---|
| Number of shares after the Capital Increase | 45,837,043 |
| Amount of the Capital Increase | EUR 392,120,658 |
| Equity of the Company after the Capital Increase | EUR 811,502,007 |
| Equity value per share after the Capital Increase | EUR 17.70 |

## 4 Statutory Auditor's report

The statutory auditor of the Company has been requested to issue a report in accordance with Articles 596 and 598 of the Belgian Companies Code.

## 5 Justification of the cancellation of the preferential subscription rights of the existing shareholders for the benefit of Gilead

The board of directors is of the opinion that the cancellation of the preferential subscription rights of the existing shareholders for the benefit of Gilead allows the Company to secure a strong and strategic partnership with Gilead in the company's interest.

## 6 Individuals, other than employees, for whose benefit the preferential subscription rights are cancelled

Within the framework of the proposed Capital Increase, the preferential subscription rights of the existing shareholders are cancelled for the benefit of Gilead Biopharmaceutics Ireland Unlimited Company, a *Private Unlimited Company* incorporated and validly existing under Irish law, with registered seat at 25/28 North Wall Quay, Dublin 1, D01H104 (Ireland) and company number 316876.

## 7 Conclusion

Taking into account the abovementioned considerations, the board of directors is of the opinion that the proposed Capital Increase in the framework of the authorized capital with cancellation of the preferential subscription rights of the existing shareholders for the benefit of Gilead is in the Company's interest.

The Capital Increase is subject to the unanimous approval by the Board of Directors' meeting to be held on or around 19 January 2016.

Made and approved on 19 January 2016

*[Signature page follows]*

[1] The equity value of the Company is based on the financial statements of Galapagos NV on a consolidated basis under IFRS per 30 September 2015, as adjusted for the capital increase of 4 December 2015.

For the Board of Directors of the Company,

| | |
|---|---|
| [Signed] | [Signed] |
| Onno van de Stolpe<br>Director | Harrold van Barlingen<br>Director |