

ACTELION LTD AND SUBSIDIARIES
INDEX TO THE CONSOLIDATED FINANCIAL STATEMENTS

Report of group auditors	2
Consolidated Statements of Operations for the years ended December 31, 2002 and 2001	3
Consolidated Balance Sheets as of December 31, 2002 and 2001	4
Consolidated Statements of Cash Flows for the years ended December 31, 2002 and 2001	5
Consolidated Statement of Changes in Shareholders' Equity for the years ended December 31, 2002 and 2001	6
Notes to the consolidated financial statements	7

Report of the group auditors
to the Board of Directors of
Actelion Ltd
Allschwil

As auditors of the group, we have audited the accompanying consolidated financial statements of Actelion Ltd and its subsidiaries, consisting of the consolidated balance sheets as of December 31, 2002 and 2001, the consolidated statements of operations, of cash flows, of changes in shareholders' equity for the years ended December 31, 2002 and 2001 and the notes to the consolidated financial statements.

These consolidated financial statements are the responsibility of the Board of Directors of Actelion Ltd. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We confirm that we meet the Swiss legal requirements concerning professional qualification and independence.

Our audit was conducted in accordance with auditing standards promulgated by the Swiss profession and auditing standards generally accepted in the United States of America, which require that an audit be planned and performed to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement. We have examined on a test basis evidence supporting the amounts and disclosures in the consolidated financial statements. We have also assessed the accounting principles used, significant estimates made and the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements presents fairly, in all material respects, the financial position of Actelion Ltd and its subsidiaries at December 31, 2002 and 2001 and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America and comply with Swiss law.

As discussed in Note 1 to the consolidated financial statements, Actelion Ltd changed its basis of accounting from International Financial Reporting Standards to accounting principles generally accepted in the United States of America. Actelion Ltd also changed its method of accounting for goodwill in 2002.

PricewaterhouseCoopers AG

Thomas Brüderlin Hans-Rudolf Tanner

Basel, 11 February 2004

ACTELION LTD AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

	<u>Note</u>	For the year ended	
		December 31,	
		<u>2002</u>	<u>2001</u>
<i>(in CHF thousands, except share and per share amounts)</i>			
Net revenue:			
Products sales.....	2	121,834	3,386
Contract revenue.....	2	18,422	15,498
Total net revenue.....		<u>140,256</u>	<u>18,884</u>
Operating expenses			
Cost of sales.....		19,329	4,276
Research and development.....		61,510	79,494
Marketing and advertising.....		57,931	24,216
Selling, general and administrative.....		47,579	32,479
Write-off of acquired in -process research and development.....	4	-	1,000
Amortization of acquired intangible assets.....	13	1,221	2,731
Total operating expense.....		<u>187,570</u>	<u>144,196</u>
Operating loss.....		<u>(47,314)</u>	<u>(125,312)</u>
Interest income.....		1,718	7,435
Interest expense.....		(694)	(219)
Other financial expense, net.....		(5,626)	(3,227)
Loss before income tax expense, minority interests and share in loss of affiliate.....		<u>(51,916)</u>	<u>(121,323)</u>
Income tax expense.....	6	(335)	(379)
Loss before minority interests and share in loss of affiliate.....		<u>(52,251)</u>	<u>(121,702)</u>
Loss (income) attributable to minority shareholders.....	7	1,286	(275)
Loss before share in loss of affiliate.....		<u>(50,965)</u>	<u>(121,977)</u>
Share in loss of affiliate.....	15	(1,092)	(946)
Net loss.....		<u>(52,057)</u>	<u>(122,923)</u>
Basic and diluted loss per share.....	8	<u>(2.45)</u>	<u>(5.98)</u>

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

**ACTELION LTD AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS**

(in CHF thousands, except share and per share amounts)

	Note	December 31,	
		2002	2001
Assets			
Current assets			
Cash and cash equivalents.....	9	116,977	92,958
Marketable securities	10	4,945	21,569
Derivative instruments	10	1,622	-
Trade and other receivables, net	11	23,949	11,338
Inventories.....	12	13,821	6,246
Other current assets.....		3,225	2,240
Total current assets.....		164,539	134,351
Marketable securities, longterm.....	10	6,898	37,663
Property, plant and equipment, net.....	14	28,411	16,037
Investment in affiliate.....	15	2,171	815
Other assets.....		3,324	3,080
Intangible assets, net	13	9,945	4,176
Goodwill, net	13	3,672	3,184
Total assets.....		218,960	199,306
Liabilities and Shareholders' Equity			
Current liabilities			
Trade and other payables.....		26,153	12,222
Accrued expenses.....	16	20,430	8,080
Deferred revenue	5	8,405	8,938
Other current liabilities.....	17, 18	923	737
Total current liabilities.....		55,911	29,977
Long-term financial debt, less current portion	17	47,460	-
Deferred revenue, less current portion.....	5	62,712	69,031
Other non-current liabilities.....	18, 19	2,063	2,239
Total liabilities.....		168,146	101,247
Minority interest	7	494	1,184
Commitments and contingencies.....	18		
Shareholders' Equity.....			
Common shares (par value CHF2.50 per share, authorized 27,456,640 and 26,908,640 shares; issued 21,376,559 and 21,134,860 shares in 2002 and 2001, respectively).....		53,441	52,837
Additional paid-in-capital.....		289,671	287,344
Accumulated deficit		(287,310)	(235,253)
Unearned compensation.....		(3,936)	(8,247)
Treasury shares, at cost.....		(1,018)	-
Accumulated other comprehensive (loss) income.....	22	(528)	194
Total shareholders' equity.....		50,320	96,875
Total liabilities, minority interest and shareholders' equity.....		218,960	199,306

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

ACTELION LTD AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the year ended	
	December 31,	
<i>(in CHF thousands)</i>	2002	2001
Cash flows from operating activities		
Net loss	(52,057)	(122,923)
Adjustments to reconcile net loss to net cash provided from operating activities:		
Minority interest	(1,286)	275
Depreciation and amortization	6,647	6,635
Share in loss of affiliate	1,092	946
Stock-based compensation	4,112	9,751
Realized loss on sale of marketable securities	1,157	4,207
Gain on derivative instruments	(924)	-
(Increase) decrease in trade and other receivables	(14,394)	51,072
Increase in inventories	(7,575)	(3,187)
Increase in other current assets	(1,135)	(1,732)
Increase in other assets	(590)	(1,297)
Increase in trade and other payables	7,716	4,306
Increase in accrued expenses	13,562	2,201
Decrease in deferred revenue	(6,852)	(1,791)
Increase in other liabilities	272	1,048
Net cash flow used by operating activities	(50,255)	(50,489)
Cash flows from investing activities		
Purchase of marketable securities	(13,235)	(9,016)
Proceeds from the sales of marketable securities	58,571	9,345
Purchase of property, plant and equipment	(17,987)	(9,303)
Purchase of intangible assets	(599)	(4,150)
Increase in investments of affiliates	(505)	(750)
Acquisition of subsidiaries	-	(2,336)
Net cash flow provided by (used in) investing activities	26,245	(16,210)
Cash flows from financing activities		
Payments on capital leases	(713)	(1,373)
Proceeds from the issuance of financial debt	47,820	-
Proceeds from the exercise of stock options	1,215	4,296
Acquisition of treasury shares	(1,018)	-
Proceeds from the sales of treasury shares	55	137
Net cash flow provided by financing activities	47,359	3,060
Net effect of exchange rates on cash and cash equivalents	670	273
Net change in cash and cash equivalents	24,019	(63,366)
Cash and cash equivalents at beginning of year	92,958	156,324
Cash and cash equivalents at end of year	116,977	92,958
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest	509	162
Taxes	462	124

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

ACTELION LTD AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

	Common Shares		Additional	Accumulated	Unearned	Treasury	Other	Shareholders'
	Shares	Amount	Paid-in-Capital	Deficit	Compensation	Shares	Comprehensive Loss	Equity
<i>(in CHF thousands, except share amounts)</i>								
At January 1, 2001	19,470,760	48,677	285,305	(112,330)	(16,241)	-	(252)	205,159
Comprehensive loss net of tax effect:								
Net loss				(122,923)				(122,923)
Other comprehensive income:								
Unrealized gain on marketable securities.....							266	266
Currency translation adjustment.....							180	180
Total comprehensive loss.....								<u>(122,477)</u>
Exercise of stock options and warrants.....	1,664,100	4,160	136					4,296
Changes in underlying equity of affiliate.....			90					90
Transactions in treasury shares.....			137					137
Stock-based compensation expense, net			1,210		8,460			9,670
Issuance of stock options.....			748		(748)			-
Stock option forfeitures and cancellations.....			(282)		282			-
At December 31, 2001	21,134,860	52,837	287,344	(235,253)	(8,247)	-	194	96,875
Comprehensive loss net of tax effect:								
Net loss				(52,057)				(52,057)
Other comprehensive loss:.....								
Unrealized loss on marketable securities.....							(263)	(263)
Currency translation adjustment.....							(459)	(459)
Total comprehensive loss.....								<u>(52,779)</u>
Changes in underlying equity of affiliate.....			1,943					1,943
Exercise of stock options.....	241,699	604	611					1,215
Transactions in treasury shares.....	(13,500)		55			(1,018)		(963)
Stock-based compensation expense, net			888		3,141			4,029
Issuance of stock options.....			1,869		(1,869)			-
Stock option forfeitures and cancellations.....			(3,039)		3,039			-
At December 31, 2002	21,363,059	53,441	289,671	(287,310)	(3,936)	(1,018)	(528)	50,320

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

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Note 1. Description of business and summary of significant accounting policies

Actelion LTD. (“Actelion” or the “Group”), a biopharmaceutical company headquartered in Allschwil, Switzerland, discovers, develops and commercializes innovative low molecular weight drugs for high unmet medical needs.

Basis of accounting

The Group’s consolidated financial statements have been prepared under accounting principles generally accepted in the United States of America (“US GAAP”) and are presented in Swiss francs (“CHF”). On October 27, 2003, the Group announced its intention to adopt US GAAP for its financial reporting and to restate all periods since inception. All periods presented are accounted for under US GAAP. Prior to the conversion the Group’s consolidated financial statements were prepared in accordance with International Financial Reporting Standards including International Accounting Standards and Interpretations as issued by the International Accounting Standards Board.

Use of estimates

The preparation of financial statements in conformity with US GAAP requires management to make judgments, assumptions and estimates that affect the amounts reported in the financial statements and accompanying notes. On an on-going basis, management evaluates its estimates, including those related to revenue recognition for contract revenue, stock based compensation, purchase accounting and impairment. The Group bases its estimates on historical experience and on various other market-specific assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ significantly from these estimates.

Principles of consolidation

The consolidated financial statements include the accounts of Actelion and its wholly-owned subsidiaries as well as affiliated companies in which the Group has a controlling financial interest and exercises control over their operations. All material intercompany transactions and balances have been eliminated in consolidation. Investments in affiliated companies which are 50% or less owned and where the Group exercises significant influence over operations are accounted for using the equity method.

Consistent with our policy for purchases or sales of equity by an investee, at the time a less than wholly-owned consolidated subsidiary sells its stock to unrelated parties at a price different than its book value, the Group’s net investment in that subsidiary changes. The Group records the resulting increase or decrease in its net investment as a gain or loss to the Group’s additional paid-in -capital.

Segment information

Statement of Financial Accounting Standards (“SFAS”) No. 131, “Disclosures about Segments of an Enterprise and Related Information”, establishes standards for reporting information on operating segments in interim and annual financial statements. The Group’s chief operating decision-makers review the profit and loss of the Group on an aggregate basis and manage the operations of the Group as a single operating segment. Accordingly, the Group operates in one segment.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Revenue recognition

Product Sales

The Group recognizes revenue from product sales when there is persuasive evidence that an arrangement exists, delivery has occurred, the price is fixed and determinable, and collectibility is reasonably assured. Allowances are established for estimated uncollectible amounts, product returns and discounts. Generally, the Group ships products to its customers fully insured with shipping terms of FOB destination point.

Contract Revenue

Contract revenue includes license fees, milestone payments associated with collaborations with third parties and clinical service revenue. Revenue from non-refundable, upfront license fees is recognized over the estimated performance or agreement period, depending on the terms of the agreement. The recognition of revenue is prospectively changed for subsequent changes in the development or agreement period. Revenue associated with performance milestones where the Group has continuing involvement is recognized upon achievement of the milestones. Clinical service revenue is recognized as the services are provided and collection is reasonably assured. Payments received in excess of amounts earned are classified as deferred revenue until earned.

Shipping and handling costs

The Group recognizes expenses relating to shipping and handling costs in cost of goods sold.

Research and development

Research and development expense consists primarily of compensation and other expenses related to research and development personnel; costs associated with pre-clinical testing and clinical trials of the Group's product candidates, including the costs of manufacturing the product candidates; expenses for research and services rendered under co-development agreements; and facilities expenses. All research and development costs are charged to expense when incurred.

Payments made to acquire research and development assets, including those payments made under licensing agreements, that are deemed to have an alternative future use or are related to proven products are capitalized as intangible assets; otherwise, they are expensed as research and development costs. For further information on payments made under the Group's licensing agreements refer to Note 4, "Licensing Agreements."

Advertising costs

The Group expenses the costs of advertising, including promotional expenses, as incurred. Advertising expenses were CHF 28.0 million in 2002 and CHF 14.1 million in 2001.

Patents and trademarks

Costs associated with the filing and registration of patents and trademarks are expensed in the period in which they occur.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Taxes

The Group uses the liability method to account for income taxes as required by SFAS No. 109, "Accounting for Income Taxes." Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities, and are measured using enacted tax rules and laws that will be in effect when differences are expected to reverse. The Group records valuation allowances to reduce deferred tax assets to the amount that is more likely than not to be realized. Significant estimates are required in determining income tax expense and benefits. Various internal and external factors may have favorable or unfavorable effects on the future effective tax rate. These factors include, but are not limited to, changes in tax laws, regulations and/or rates, changing interpretations of existing tax laws or regulations, future levels of capital expenditures, and changes in overall levels of pretax earnings.

Loss per share

Basic loss per share is computed using the weighted average number of common shares outstanding during the period. Diluted loss per share is computed using the weighted average number of common and diluted common equivalent shares outstanding during the period using the treasury stock method for options, unless amounts are anti-dilutive.

Dividends

The Group may declare dividends upon the recommendation of the board of directors and the approval of shareholders at their annual general meeting. Under Swiss corporate law, the Group's right to pay dividends may be limited in specific circumstances. The Group has not paid any cash dividends since inception and does not anticipate a dividend in the near to medium term.

Cash and cash equivalents

The Group considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents. Additionally, the Group includes all amounts held in money market funds as cash equivalents.

Marketable securities

The Group categorizes marketable securities as either "available-for-sale" or "held-to-maturity." Available-for-sale securities are carried at fair value with unrealized gains and losses recorded as a separate component of shareholders' equity. Held-to-maturity securities are carried at amortized cost. Dividends and interest income are accrued as earned. Realized gains and losses are determined on an average cost basis. The Group reviews marketable securities for impairment whenever circumstances and situations change, such that there is an indication that the carrying amounts may not be recovered. Securities with unrealized losses for more than six months are presumed to be impaired, absent compelling evidence to the contrary. In addition, securities with unrealized losses for less than six months may be deemed impaired in certain circumstances.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Derivative instruments

A significant portion of the Group's operations is denominated in foreign currencies, principally in U.S. dollars and Euros. The inherent exposure may adversely impact the Group's net income and net assets. The Group uses derivatives to partially offset market exposure to fluctuations in foreign currencies. The Group records all derivatives on the balance sheet at fair value. The Group's derivative instruments, while providing effective economic hedges under the Group's policies, do not qualify for hedge accounting as defined by SFAS No.133, "Accounting for Derivative Instruments and Hedging Activities". Changes in the fair value of any derivative instruments are recognized immediately in other financial expense in the consolidated statements of operations. See the Note 10, "Derivative Financial Instruments" below for further information on the Group's accounting for derivatives.

The Group does not regularly enter into agreements containing embedded derivatives. However, when such agreements are executed, an assessment is made of any embedded derivative based on the criteria outlined in SFAS No. 133 to determine if the derivative is required to be bifurcated and accounted for separately. As of December 31, 2002, the Group had such derivatives in its short-term and long-term bonds. See Note 10, "Investments" below for further information on the Group's accounting for these embedded derivatives.

Accounts receivable

The Group maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. If the financial condition of the Group's customers were to deteriorate, resulting in an impairment of their ability to make payments, an increase to the allowance may be required, which could affect future earnings.

Inventories

Inventories are stated at the lower of cost or market with cost determined by the first-in first-out (FIFO) method. Inventories consist of intermediaries and finished products. If inventory costs exceed the expected market value due to obsolescence or unmarketability, a reserve is recorded for the difference between the cost and the market value.

Investments in affiliates

Investments in which the Group is able to exercise significant influence over the investee company are accounted for under the equity method of accounting. Under this method, the investment balance, originally recorded at cost, is adjusted to recognize the Group's share of net earnings or losses of the investee company as they occur, limited to the extent of the Group's investment in, advances to and commitments to the investee. These adjustments are reflected in equity in losses of affiliates in the consolidated statements of operations.

At the time an equity method investee sells its stock to unrelated parties at a price in excess of its book value, the Group's net investment in that affiliate increases. If at that time, the affiliate is a newly formed, non-operating entity, a research and development company, start-up or development stage company, and if there is a question as to the ability to realize the gain in the future, the Group records the increase as an gain to the Group's additional paid-in-capital.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Property, plant and equipment

Property, plant and equipment is recorded at historical cost less accumulated depreciation.

Depreciation expense is recorded utilizing the straight-line method over the estimated useful life of the asset. Assets are written down to their estimated residual value. Leasehold improvements and assets acquired under capital leases are amortized using the straight-line method over the shorter of the lease term or estimated useful life of the asset. Assets acquired under capital leases in which title transfers to the Group at the end of the agreement are amortized over the useful life of the asset. Expenditures for maintenance and repairs are charged to expense as incurred.

The depreciation periods in years are as follows:

Group of assets	Useful life
Computers.....	3 years
Furniture and fixtures.....	5 years
Laboratory equipment.....	5 years
Leasehold improvements.....	6 to 10 years

The carrying value of the Group's long-lived assets is reviewed for impairment whenever events or changes in circumstances indicate that the asset may not be recoverable. Specific potential indicators of impairment include:

- a significant decrease in the fair value of an asset;
- a significant change in the extent or manner in which an asset is used or a significant physical change in an asset;
- a significant adverse change in legal factors or in the business climate that affects the value of an asset;
- an adverse action or assessment by the U.S. Food and Drug Administration or another regulator;
- an accumulation of costs significantly in excess of the amount originally expected to acquire or construct an asset; and
- operating or cash flow losses combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with an income-producing asset.

Should there be indication of impairment, an assessment will be made by comparing the estimated future cash flows expected to result from the use of the asset and its eventual disposition to the carrying amount of the asset. In estimating these future cash flows, assets are grouped at the lowest level for which there are identifiable cash flows that are largely independent of the cash flows generated by other asset groups. If the sum of the expected future cash flows (undiscounted and without interest changes) is less than the carrying amount of the asset, an impairment loss, measured as the excess of the carrying value of the asset over its fair value, will be recognized. The cash flow estimates used in such calculations are based on management's best estimates, using appropriate and customary assumptions and projections at the time.

Goodwill and intangible assets

Goodwill represents the excess of purchase price over fair value of net assets acquired in a business combination. Prior to the adoption of SFAS No. 142 discussed in Note 13, goodwill was amortized on a straight-line basis over the expected benefit period, which was 3 years. The carrying value of goodwill was regularly reviewed by evaluating the estimated future undiscounted cash flows to determine recoverability of the assets.

Intangible assets consist primarily of acquired existing licenses and internal use software, which is amortized on a straight-line basis over the economic lives of the respective assets, estimated at 11 and 3 years, respectively.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Adoption of SFAS No.141 and SFAS No. 142

Effective January 1, 2002, the Group completed the adoption of SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 141 requires all business combinations initiated after June 30, 2001, to be accounted for using the purchase method of accounting. As required by SFAS No. 142, the Group discontinued amortizing the remaining balances of goodwill as of January 1, 2002. All remaining and future acquired goodwill will be subject to impairment tests annually, or earlier if indicators of potential impairment exist, using a fair-value-based approach. All other intangible assets will continue to be amortized over their estimated useful lives and assessed for impairment under SFAS No. 142. In conjunction with the implementation of SFAS No. 142, the Group has completed an initial and annual goodwill impairment test in 2002 and found no impairment. If the Group determines that a potential impairment of goodwill exists, the Group will perform the impairment measurement procedures under SFAS No. 142 which may result in a charge for the impairment of goodwill in future periods. The transitional disclosures required by SFAS No. 142 are included in Note 13.

Adoption of SFAS No. 144

On January 1, 2002, the Group adopted SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". Long-lived assets, such as property and equipment, and definite-lived intangibles are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell, and depreciation ceases. Prior to the adoption of SFAS No. 144, the Group accounted for impairment of long-lived assets and long-lived assets to be disposed of in accordance with SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of". The adoption of SFAS No. 144 has not had a material impact on the Group's consolidated financial position or results of operations.

Stock-based compensation

The Group accounts for stock-based awards to employees and directors using the intrinsic value method in accordance with APB No. 25, "Accounting for Stock Issued to Employees." Accordingly, the Group does not recognize compensation expense for employee stock options granted with an exercise price equal to the market value of the underlying common stock at the date of grant. In instances where an option is granted to an employee with an exercise price below the market value of the underlying common stock at the date of grant, the option is expensed in accordance with Financial Accounting Standards Board ("FASB") Interpretation Number 28, "Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans an interpretation of APB Opinions No. 15 and 25." For purposes of disclosures pursuant to SFAS No. 123 as amended by SFAS No. 148, the estimated fair value of options is amortized to expense over the options' vesting period. Equity instruments issued to non-employees are measured at fair value over the period of performance using the Black-Scholes option pricing model.

Comprehensive loss

Comprehensive loss is comprised of net loss and other comprehensive income (loss). Other comprehensive income (loss) includes unrealized gains and losses on available-for-sale securities and currency translation adjustments. Comprehensive loss for the years ended December 31, 2002 and 2001 has been reflected in the consolidated statement of changes in shareholders' equity.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Foreign currency exposure

Income, expense and cash flows of foreign subsidiaries are translated into the Group's reporting currency at quarterly average exchange rates and the corresponding balance sheets translated at the period-end exchange rate. Exchange differences arising from the translation of the net investment in foreign subsidiaries and long-term internal financing are recorded, net of tax, in "Cumulative Translation Adjustment" in shareholders' equity.

Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transactions. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognized in the subsidiary's statement of operations in the corresponding period.

Interest rate risk

Interest rate risk arises from movements in interest rates, which could have adverse effects on the Group's net income or financial position. Changes in interest rates cause variations in interest income and expenses on interest-bearing assets and liabilities. In addition, they can affect the market value of certain financial assets, liabilities and instruments.

Recent accounting pronouncements

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," which addresses accounting for restructuring, plant closing, or other exit or disposal activity. SFAS 146 requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. SFAS 146 is to be applied prospectively to exit or disposal activities initiated after December 31, 2002. The adoption of SFAS 146 is not expected to have a significant impact on financial position and results of operations.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity". SFAS No. 150 establishes standards on the classification and measurement of financial instruments with characteristics of both liabilities and equity. SFAS No. 150 is effective for financial instruments entered into or modified after May 31, 2003. The adoption of this accounting pronouncement will not have a material effect on the Group's results of operations, cash flows or financial position.

In November 2002, the FASB issued Interpretation No. 45 ("FIN 45"), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." FIN 45 elaborates on the existing disclosure requirements for most guarantees, including residual value guarantees issued in conjunction with operating lease agreements. It also clarifies that at the time a company issues a guarantee, the company must recognize an initial liability for the fair value of the obligation it assumes under that guarantee and must disclose that information in its interim and annual financial statements. The initial recognition and measurement provisions apply on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure requirements are effective for financial statements of interim or annual periods ending after December 15, 2002. The adoption of FIN 45 did not have a material impact on financial position and results of operations.

In January 2003, the FASB issued Interpretation No. 46 ("FIN 46"), "Consolidation of Variable Interest Entities." FIN 46 requires a variable interest entity to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. A variable interest entity is a corporation, partnership, trust, or any other legal structures used for business purposes that either (a) does not have equity investors with voting rights or (b) has equity investors that do not provide sufficient financial resources for the entity to support its activities. A variable interest entity often holds financial assets, including loans or receivables, real estate or other property. A variable interest entity may be essentially passive or it may engage in research and development or other activities on behalf of another company. The consolidation requirements of FIN 46 apply immediately to variable interest entities created after January 31, 2003. The consolidation requirements apply to older entities in the first fiscal year or interim period beginning after

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

June 15, 2003. Certain of the disclosure requirements apply to all financial statements issued after January 31, 2003, regardless of when the variable interest entity was established. The Group has not identified any variable interest entities, therefore, the adoption of FIN 46 is not expected to have a material impact on financial position and results of operations.

In November 2002, the Emerging Issues Task Force ("EITF") issued Issue No. 00-21, "Revenue Arrangements with Multiple Deliverables." EITF Issue No. 00-21 addresses certain aspects of the accounting by a company for arrangements under which it will perform multiple revenue-generating activities. EITF Issue No. 00-21 addresses when and how an arrangement involving multiple deliverables should be divided into separate units of accounting. EITF Issue No. 00-21 provides guidance with respect to the effect of certain customer rights due to company nonperformance on the recognition of revenue allocated to delivered units of accounting. EITF 00-21 also addresses the impact on the measurement and/or allocation of arrangement consideration of customer cancellation provisions and consideration that varies as a result of future actions of the customer or the company. Finally, EITF Issue No. 00-21 provides guidance with respect to the recognition of the cost of certain deliverables that are excluded from the revenue accounting arrangement. The provisions of EITF Issue No. 00-21 will apply to revenue arrangements entered into in fiscal periods beginning after June 15, 2003. EITF 00-21 is not expected to have a material impact on adoption.

In May 2003, the EITF issued Issue No. 01-08, "Determining Whether an Arrangement Contains a Lease." EITF Issue 01-08 provides guidance in determining whether an arrangement should be considered a lease subject to the lease accounting and disclosure guidance of FASB Statement No. 13, "Accounting for Leases". The provisions of EITF Issue 01-08 apply to both potential lessors and lessees that have agreed or committed to arrangements, modified arrangements, or acquired arrangements in business combinations initiated after the beginning of the reporting period following May 28, 2003. The Group is in the process of assessing the impact that EITF Issue 01-08 will have on the financial statements.

In December 2003, the FASB issued SFAS No. 132 (revised 2003), "Employers' Disclosures about Pensions and Other Postretirement Benefits". This Statement establishes standards on additional disclosures to those in the original Statement No. 132 about the assets, obligations, cash flows, and net periodic costs of defined benefit pension plans and other postretirement benefit plans separately for pension plans and other postretirement benefit plans. SFAS No. 132 (revised 2003) is effective for financial statements with fiscal years ending after December 15, 2003. The effects of this standard will not have a material impact on adoption.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Note 2. Segment And Geographic Information

The Group operates in one segment, which is the business of discovering, developing and commercializing drugs for human health care. The chief operating decision makers review the profit and loss of the Group on an aggregate basis and manage the operations of the Group as a single operating segment. The Group currently derives product revenue from sales of its product Tracleer for the treatment of pulmonary arterial hypertension. Contract revenue is derived from collaboration and service agreements with third parties. Product revenue attributable to individual countries is based on location of the customer.

The Group's geographic information is as follows:

December 31, 2002:	Switzerland	United States	Europe	Other	Total
Product revenue from external customers.....	3,769	87,265	25,422	5,378	121,834
Contract revenue from external customers	18,422	-	-	-	18,422
Long-lived assets.....	36,074	1,256	3,557	1,141	42,028
December 31, 2001:	Switzerland	United States	Europe	Other	Total
Product revenue from external customers.....	-	2,453	933	-	3,386
Contract revenue from external customers	15,489	-	9	-	15,498
Long-lived assets.....	18,127	1,983	2,644	643	23,397

Note 3. Acquisitions

Hesperion AG

During 1999, the Group acquired 70% of the voting stock of Hesperion AG ("Hesperion"), a privately-held company in Switzerland with expertise in conducting clinical trials. This acquisition was recorded as a purchase business combination. The Group's share in Hesperion was changed as a result of Hesperion's issuances and repurchases of additional shares. In December 2002, the Group acquired an additional 5% of the voting stock of Hesperion for CHF 520,039, including CHF 21,000 of transaction related costs. The Group increased its interest to maintain a controlling interest and to further capitalize Hesperion.

The fair-value of the net assets acquired were not materially different than the carrying values of those assets. As a result, the entire purchase price of CHF 520,039 for the additional 5% of the voting stock of Hesperion was allocated to goodwill. The pro forma effects of this acquisition were not materially different than actual results.

Associate Statistical Consultants S.r.l.

On January 1, 2001, the Group acquired all of the outstanding shares of Associate Statistical Consultants S.r.l. ("ASC"), a privately-held company, for CHF 2.34 million, including CHF 18,000 of transaction related costs. ASC is a biometrical company with dedicated resources specializing in the field of statistical analysis. The acquisition was recorded as a purchase business combination, and accordingly, the operating results of ASC are included in the accompanying consolidated financial statements starting from January 2, 2001. The Group acquired ASC for its know-how and additional resources to be used in clinical trials.

The purchase price was allocated among identifiable tangible and intangible assets and liabilities of ASC based upon their estimated fair values. The excess of the purchase price over the fair value of assets and liabilities acquired of CHF 2.28 million was allocated to goodwill, which was amortized through December 31, 2001 using a 3-year useful life. Goodwill amortization ceased beginning January 1, 2002 in accordance with SFAS No. 142.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Note 4. Licensing Agreements

On March 19, 1998, the Group entered into a license agreement with F. Hoffman-La Roche (“Roche”) for tezosentan. Under this agreement, Roche granted the Group an exclusive worldwide right to manufacture and sell any product with tezosentan as its active ingredient. The license covers any human therapeutic use of tezosentan except acute renal failure and subarachnoid hemorrhage. The Group may also grant sub-licenses to third parties. The agreement called for the Group to make an initial payment to Roche as well as payments upon the achievement of certain milestones. The Group will make milestone payments upon the filing and approval of new drug applications in the United States and the European Union. If the Group is successful in obtaining regulatory approval for Veletri, the Group will pay a royalty to Roche based on a percentage of net sales of products with tezosentan as the active ingredient. No payments were made under this agreement during 2002 and 2001.

On November 4, 1998 the Group entered into a license agreement with Roche for bosentan, the active ingredient in the Group’s product, Tracleer. The license grants the Group the exclusive worldwide rights to develop, manufacture, sell any pharmaceutical product with bosentan as its active ingredient for any human therapeutic use, and grant sub-licenses to third parties. The agreement called for the Group to make an initial payment to Roche as well as payments upon the achievement of certain milestones. All payments made to Roche prior to receiving regulatory approval were expensed as acquired in-process research and development costs. Payments made to Roche subsequent to receiving regulatory approval were capitalized and are being amortized over the life of the agreement. As of December 31, 2002 and 2001, CHF 9 million and CHF 2.5 million, respectively, is included in intangible assets and is being amortized over 11 years. During 2001, the Group made payments of CHF 1 million under this agreement which were expensed as acquired in-process research and development costs. The agreement also calls for the Group to pay a royalty to Roche based on a percentage of net sales of products with bosentan as the active ingredient. In 2002, the Group reached agreement with Roche to delay payment of CHF 9 million until March 31, 2003 of its 2002 obligation under the license agreement for Bosentan. In accordance with this new agreement the Group will pay interest equal to LIBOR plus 1%. These amounts are recorded in other payables.

On November 22, 2002 the Group entered into a license agreement with Oxford GlycoSciences (“OGS”) for miglustat, the active ingredient of Zavesca. OGS has since been acquired by Celltech Group plc. In 1998, OGS in-licensed miglustat from G.D. Searle & Co. Under the Group’s license agreement with OGS, the Group has been granted exclusive marketing rights to sell Zavesca in all countries except Israel and the adjacent West Bank and Gaza Strip territories. For the period from January 1, 2003 through the expiration of the agreement, the Group will pay OGS a royalty on net sales of Zavesca. The agreement also provides that OGS will be the Group’s sole supplier of Zavesca. As of December 31, 2002 no royalties were paid under this agreement.

Note 5. Collaborative Agreements

In July 1999, the Group entered into an agreement with a subsidiary of Johnson and Johnson (“J&J”). For the first three years of the agreement, J&J paid the Group for certain research and development costs incurred under the agreement. For the years ended December 31, 2002 and 2001 the Group recognized revenue of CHF 3.9 million and CHF 5.4 million, respectively. In addition, J&J is obligated to make payments to the Group on the achievement by J&J of certain milestones.

In February 2000, the Group entered into an agreement with Genentech Inc. (“Genentech”) for the co-exclusive, royalty-bearing right and license to research, develop, manufacture and sell tezosentan in the United States. Genentech may elect to co-promote the drug for certain indications in the United States or receive a royalty on net sales of tezosentan in the United States. Upon signing the contract the Group received an upfront payment, which is being recognized over the life of the agreement. For the years ended December 31, 2002 and 2001 the Group recognized revenue of CHF 1.5 million related to this agreement.

In December 2000, the Group entered into an agreement with Genentech for the co-exclusive, royalty-bearing right and license to research, develop, manufacture and sell bosentan, the active ingredient in Tracleer, in the United States. Genentech receives a royalty on net sales of bosentan in the United States. Upon signing the contract the Group received an upfront payment, a portion of which was refundable if the Group did not complete Phase III trials

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

for bosentan for use in the treatment of chronic heart failure. The non-refundable portion of the upfront payment is being recognized over the agreement period, which began in December 2000. In December 2001 the Group received FDA approval for bosentan in the United States for the treatment of pulmonary arterial hypertension and began paying Genentech a royalty on net sales. In January 2002 the Group completed Phase III trials for bosentan for the use in the treatment of chronic heart failure and received neutral results. Upon completion of Phase III trials and receipt of the neutral results, the Group began recognizing the refundable portion of the upfront payment over the remaining agreement period. For the years ended December 31, 2002 and 2001, the Group recognized revenue of CHF 4.9 million and CHF 3.4 million respectively, under this agreement.

Note 6. Income taxes

The following table sets forth the components of the provision for income taxes:

	For the Year Ended	
	December 31,	
	2002	2001
Current tax expense:		
Switzerland	222	359
Foreign	113	20
Total current tax expense	335	379

The following table sets forth the components of loss before income taxes, minority interests and share in loss of affiliate by jurisdiction:

	For the Year Ended	
	December 31,	
	2002	2001
Switzerland	21,581	93,569
Foreign	30,335	27,754
Total	51,916	121,323

The Group is located in Switzerland which has a statutory income tax rate of 25%. The difference between the statutory rate and the effective rate for 2002 and 2001 is primarily a result of the valuation allowance on deferred tax assets.

Significant components of the Group's deferred tax assets as of December 31, 2002 and 2001 are shown below. A valuation allowance of CHF 48.3 million of which CHF 11.0 million is related to 2002, has been recognized because of the Group's historical cumulative operating losses. The Group has CHF 153.5 million of tax loss carryforwards which expire between 3 and 5 years.

	2002	2001
Deferred tax assets:		
Net benefit from operating loss carryforwards	35,866	24,306
Deferred revenue	10,700	10,686
Other	1,767	2,332
Total deferred tax assets	48,333	37,324
Valuation allowance for deferred tax assets	(48,333)	(37,324)
Net deferred tax assets	-	-

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Note 7. Minority interests

The Groups' share in Hesperion was increased in December 2002 from 69% to 74% as a result of the issuance of additional shares. Minority interests at December 31, 2002 consist of 26% of Hesperion and are held by Hesperion management and employees. The following table shows changes in the minority interest since January 1, 2001:

	<u>2002</u>	<u>2001</u>
January 1	1,184	828
Change in minority interest due to capital transaction.....	602	80
Change in minority interest due to result of the year.....	(1,286)	275
Change in translation adjustment	(6)	1
December 31	<u>494</u>	<u>1,184</u>

Note 8. Loss Per Share

For the years ended December 31, 2002, and 2001, loss per basic and diluted share are based on weighted average common shares and exclude diluted shares of 951'590 and 1'315'201, respectively, relating to employee stock options, as they would be anti-dilutive due to the reported losses.

	<u>2002</u>	<u>2001</u>
Net loss.....	(52,057)	(122,923)
Weighted average number of shares outstanding.....	21,282,433	20,561,372
Basic and diluted loss per share	(2.45)	(5.98)

Note 9. Cash and cash equivalents

Cash and cash equivalents consisted of the following at December 31, 2002 and 2001:

	<u>2002</u>	<u>2001</u>
Cash	46,736	35,189
Short-term bank deposits.....	69,665	51,824
Money market funds.....	576	5,945
Total	<u>116,977</u>	<u>92,958</u>

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Note 10. Investments

Marketable Securities

The following is a summary of marketable securities at December 31:

	2002			2001				
	Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value	Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Available-for-sale securities:								
Short-term equity securities	94			94	22,377	363	(1,171)	21,569
Long-term debt securities					36,592	1,425	(354)	37,663
Total Available-for-Sale Securities	94	-	-	94	58,969	1,788	(1,525)	59,232
Held-to-maturity securities:								
Short-term bond	4,851			4,851	-			-
Long-term bond	6,898			6,898	-			-
Total Held-to-maturity securities	11,749			11,749	-			-
Total Marketable Securities	11,843	-	-	11,843	58,969	1,788	(1,525)	59,232

The Group's held-to-maturity debt securities have the following maturities at December 31, 2002:

	Held-to- maturity
Due in less than one year	4,851
Due in more than one year but less than five years	6,898
Total	11,749

The unrealized gains and losses as of December 31, 2002 and 2001 were reported as accumulated other comprehensive loss, which is a separate component of stockholders' equity. Realized gains and losses on available-for-sale securities for 2002 and 2001 included the following:

	2002		2001	
	Realized Gains	Realized Losses	Realized Gains	Realized Losses
Available-for-sale securities:				
Short-term equity securities	639	(2,940)	99	(4,644)
Long-term debt securities	1,589	(389)	412	(75)
Total Available-for-Sale Securities	2,228	(3,329)	511	(4,719)

For the years ended December 31, 2002 and 2001, the Group recognized other-than-temporary impairments of its available-for-sale securities of CHF 0.05 million and CHF 4 million, respectively.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

For the years ended December 31, 2002 and 2001, unrealized gains and losses on available-for-sale securities that were reclassified out of accumulated other comprehensive income into other financial expense in the consolidated statements of operations included the following:

	2002		2001	
	Gains	Losses	Gains	Losses
Available-for-sale securities:				
Short-term equity securities	363	(1,171)	109	(369)
Long-term debt securities	1,425	(354)	187	(70)
Total Available-for-Sale Securities	1,788	(1,525)	296	(439)

Financial Instruments

The following tables show the contract or underlying principal amounts and fair values of derivative financial instruments at December 31, 2002 and 2001. Contract or underlying principal amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. The fair values are determined by the markets or standard pricing models at December 31, 2002. The Group held no derivative financial instruments at December 31, 2001.

<u>Derivative financial instruments</u>	Contract or underlying principal amount	Positive fair values	Negative fair values
	<u>2002</u>	<u>2002</u>	<u>2002</u>
Forward foreign exchange rate contracts.....	88,130	1,180	64
Embedded interest rate derivatives		442	
Total	88,130	1,622	64

The Group's held-to-maturity short-term bond and long-term bond mature on December 19, 2003 and December 20, 2004, respectively, and bear interest at a rate that is linked to the Equity Stoxx 50 Index. Market risks associated with these notes include equity price risk, in that the amount that the Group will receive at maturity depends on the performance of the Equity Stoxx 50 Index. As such, these notes contain an embedded derivative. Changes in the fair value of the embedded derivatives are recognized in earnings, as they do not meet the definition of a hedge.

Note 11. Trade and Other Receivables

Trade and other receivables consisted of the following at December 31:

	<u>2002</u>	<u>2001</u>
Trade receivables	21,408	4,579
Less: Allowance for doubtful accounts	(182)	(70)
Trade receivables, net	21,226	4,509
Other receivables	2,723	6,829
Total	23,949	11,338

For the year ended December 31, 2002, the Group recorded bad debt expense of CHF 112,000.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Note 12. Inventories

Inventories consisted of the following at December 31:

	<u>2002</u>	<u>2001</u>
Intermediaries.....	9,667	5,566
Finished products.....	4,154	680
Total.....	<u>13,821</u>	<u>6,246</u>

Note 13. Goodwill And Other Intangible Assets

Changes in the net carrying amount of goodwill in 2002 are as follows:

<u>Balance at January 1</u>	<u>Translation effects</u>	<u>Additions</u>	<u>Balance at December 31</u>
3,184	(32)	520	3,672

The other intangible assets consisted of the following at December 31:

	<u>2002</u>			<u>2001</u>		
	<u>Gross Carrying Amount</u>	<u>Accumulated Amortization</u>	<u>Net Carrying Amount</u>	<u>Gross Carrying Amount</u>	<u>Accumulated Amortization</u>	<u>Net Carrying Amount</u>
Acquired licenses	9,000	(506)	8,494	2,500	-	2,500
Acquired software and other.....	2,487	(1,036)	1,451	1,997	(321)	1,676
Total.....	<u>11,487</u>	<u>(1,542)</u>	<u>9,945</u>	<u>4,497</u>	<u>(321)</u>	<u>4,176</u>

Amortization expense of goodwill and other intangible assets are as follows:

	<u>2002</u>	<u>2001</u>
Goodwill amortization.....	-	2,424
Other intangible assets amortization.....	1,221	307
Total amortization expense.....	<u>1,221</u>	<u>2,731</u>

The expected future annual amortization expense of other intangible assets is as follows:

For the year ending December 31,	<u>Amortization Expense</u>
2003	1,600
2004	1,600
2005	900
2006	900
2007	900
Thereafter.....	4,045
Total expected future amortization	<u>9,945</u>

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

A reconciliation of previously reported net income and earnings per share to the amounts adjusted for the exclusion of goodwill amortization is as follows:

	December 31,	
	2002	2001
Reported net loss	(52,057)	(122,923)
Goodwill amortization	-	2,424
Adjusted net loss	(52,057)	(120,499)
Reported basic and diluted loss per share	(2.45)	(5.98)
Goodwill amortization	-	.12
Adjusted basic and diluted loss per share	(2.45)	(5.86)

Note 14. Property, plant and equipment

Property, plant and equipment consisted of the following at December 31:

	2002	2001
At cost:		
Land	342	-
Buildings	12,242	-
Furniture and fixtures and lab equipment	21,259	17,788
Computers	5,973	4,283
Other tangible assets	549	524
Less: accumulated depreciation and amortization	(11,954)	(6,558)
Property, plant and equipment, net	28,411	16,037

Depreciation expense was CHF 5.4 million in 2002 and CHF 3.9 million in 2001.

Note 15. Investment in affiliate

The movements in the Group's investment in Axovan Ltd consisted of the following:

	2002	2001
Investment at January 1,	815	921
Additional investment	505	750
Share in loss	(1,092)	(946)
Increase in underlying equity	1,943	90
Investment at December 31,	2,171	815
Ownership percentage at end of year	8.7%	22.7%

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Note 16. Accrued Expenses

Accrued expenses consisted of the following at December 31:

	<u>2002</u>	<u>2001</u>
Personnel and compensation costs	8,611	3,605
Marketing and royalties	5,767	2,610
Research and development expense.....	3,483	859
Other accrued expenses	2,569	1,006
Total	<u>20,430</u>	<u>8,080</u>

Note 17. Borrowings

	<u>At December 31, 2002</u>	
	<u>Total</u>	<u>Due within one year</u>
Borrowings from banks	40,000	-
Mortgage.....	7,820	360
Total	<u>47,820</u>	<u>360</u>

In October 2002, the Group entered into a CHF 40 million financing agreement expiring on December 31, 2004 to finance its working capital needs. The Group's obligations under this financing agreement are secured by certain of the Group's cash and cash equivalents and trade receivables. In November 2003, the Group's financing agreement was amended to eliminate the requirement for the Group to meet certain financial covenants. The amended financing agreement maintains certain reporting covenants. The Group was in compliance with all covenants under this agreement at December 31, 2002. The interest rate on this financing is set at the six-month LIBOR (London Inter-Bank Offering Rate) plus 1.5%. The fair value of this obligation at December 31, 2002 approximates the carrying value.

In 2002, the Group acquired a building and financed the purchase through a mortgage for CHF 7.8 million. The Group pays interest under the mortgage at rates ranging from 3.6% to 5%. The Group is required to make equal quarterly payments until 2024. Current maturities of this obligation are included in other current liabilities. The mortgage is collateralized by the building. The fair value of this debt at December 31, 2002 is CHF 7.7 million.

At December 31, 2002 and 2001, the Group also had unused lines of credit totaling CHF 2 million and CHF 1 million, respectively. The lines of credit bear interest rates of 5.5% and 5.8% on the outstanding balance, for the years ended December 31, 2002 and 2001, respectively.

At December 31, 2002 the aggregate amounts of indebtedness maturing during the next five years and thereafter are as follows:

Year ending December 31,	<u>Debt Financings</u>
2003.....	360
2004.....	40,360
2005.....	360
2006.....	360
2007.....	360
Thereafter.....	6,020
Total	<u>47,820</u>

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Note 18. Lease Commitments

Capital Leases

The following assets acquired under capital leases are included in property, plant and equipment:

	<u>2002</u>	<u>2001</u>
Laboratory equipment.....	4,239	4,239
Computers and software	283	181
Other tangible assets	32	-
Less: accumulated depreciation and amortization	(2,986)	(2,096)
Net assets leased under capital leases.....	<u>1,568</u>	<u>2,324</u>

The Group records interest expense relating to capital leases on a straight-line basis, which is not materially different from interest expense calculated using the imputed interest method.

Operating Leases

The Group has several operating leases for its office and research and development facilities and equipment around the world, including the Group's most significant facilities in Switzerland, the United States and Japan. The leases expire between 2003 and 2009, most of them with options to extend for 1 to 5 years. The aggregate of the minimum annual operating lease payments are expensed on a straight-line basis over the term of the related lease. The amount by which straight-line rent expense differs from actual lease payments is recognized as either prepaid rent or deferred rent liability and is reduced in later years.

Future minimum payments under noncancelable operating and capital leases at December 31, 2002 are as follows:

Year ended December 31,	<u>Operating Leases</u>	<u>Capital Leases</u>
2003.....	7,829	530
2004.....	8,226	71
2005.....	8,168	30
2006.....	7,365	12
2007.....	7,084	4
Thereafter	5,390	-
Total minimum payments	<u>44,062</u>	<u>647</u>
Less amounts representing interest.....		51
Present value of future debt payments		<u>596</u>
Less current portion of debt.....		495
Non-current portion of debt		<u>101</u>

Rent expense under operating leases was CHF 6.2 million and CHF 6.7 million for the years ended December 31, 2002 and 2001, respectively.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Note 19. Retirement Plans

The Group maintains a pension plan covering all of its employees in Switzerland including its executive officers. In addition to retirement benefits, the plan provides benefits on death or long-term disability of its employees. The Group and its employees pay retirement contributions, which are defined as a percentage of the employees' covered salaries, to a collective pension fund operated by an insurance company. Interest is credited to the employees' accounts at the minimum rate provided in the plan, payment of which is guaranteed by an insurance contract, which represents the plan's primary asset. Net periodic benefit costs for the Group's defined benefit retirement plans for 2002 and 2001 include the following components:

	<u>2002</u>	<u>2001</u>
Service cost.....	2,936	2,324
Interest cost.....	873	547
Expected return on plan assets	(707)	(413)
Amortization of net transition amount.....	97	97
Net periodic pension cost.....	<u>3,199</u>	<u>2,555</u>

The following tables provide the weighted-average assumptions used to develop net periodic benefit cost and the actuarial present value of projected benefit obligations:

	<u>2002</u>	<u>2001</u>
Weighted average discount rate	3.50%	3.50%
Expected long-term rate of return on plan assets	4.00%	4.00%
Rate of increase in compensation levels (salary)	2.00%	2.00%
Rate of increase in compensation levels (annuities).....	1.00%	1.00%

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

The following tables set forth the change in benefit obligations and change in plan assets at year-end 2002 and 2001 for the Group's defined benefit plans:

	<u>2002</u>	<u>2001</u>
Change in Projected Benefit Obligation		
Projected Benefit obligation – beginning of year.....	20,086	11,764
Service cost.....	2,936	2,324
Interest cost.....	873	547
Plan participant contributions.....	1,926	1,541
Actuarial loss.....	(70)	(47)
Transfers in	4,181	5,020
Transfers out.....	(4,294)	(1,063)
Projected Benefit obligation – end of year	<u>25,638</u>	<u>20,086</u>
Change in Plan Assets		
Plan assets at fair value – beginning of year.....	17,683	10,316
Actual return on plan assets	939	(589)
Group contributions.....	2,991	2,458
Plan participant contributions.....	1,926	1,541
Transfers in	4,181	5,020
Transfers out.....	(4,294)	(1,063)
Plan assets at fair value – end of year	<u>23,426</u>	<u>17,683</u>

Amounts recognized in the Group's balance sheet consist of the following:

	<u>2002</u>	<u>2001</u>
Plan assets less than projected benefit obligation	(2,212)	(2,403)
Unrecognized actuarial losses/(gains).....	651	954
Unrecognized net transition asset.....	97	193
Total recognized in the consolidated balance sheet.....	<u>(1,464)</u>	<u>(1,256)</u>

The liability in the consolidated balance sheet represents the difference between the cash surrender value of the insurance policy and the actuarial determined projected benefit obligation.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

The accumulated benefit obligation, project benefit obligation and the plan assets at fair value consisted of the following:

	<u>2002</u>	<u>2001</u>
Accumulated benefit obligation	23,956	18,712
Projected benefit obligation	25,638	20,086
Plan assets at fair value	23,426	17,683

Certain of the Group's subsidiaries sponsor defined contribution plans. Total contribution expense to these plans in 2002 and 2001 was CHF 983,255 and CHF 432,654, respectively. The contribution payable at December 31, 2002 and 2001, was CHF 277,755 and CHF 105,150, respectively.

Note 20. Shareholders' Equity

Authorized Capital

The Annual General Meeting of April 19, 2002, authorized an increase in share capital to be used for strategic purposes. The Board of Directors is authorized to increase until April 19, 2004 the share capital by an amount of not more than CHF 3 million by issuance of not more than 1.2 million fully paid-in registered shares with a nominal value of CHF 2.50 per share.

Conditional Capital

Since inception, the Group has created conditional capital for the establishment of stock option plans, convertible bonds as well as for the potential issuance of shares in relation with certain credit facilities. At December 31, 2002, the Group has conditional capital of CHF 12.2 million.

Movements in conditional capital are as follows:

January 1, 2001	12,314
Creation of conditional capital for employee stock option plans	500
Creation of conditional capital for convertible bonds/loans	780
Exercise of options and warrant.....	<u>(4,160)</u>
December 31, 2001	<u>9,434</u>
Creation of conditional capital for employee stock option plans.....	1,250
Creation of conditional capital for convertible bonds/loans	2,120
Exercise of options.....	<u>(604)</u>
December 31, 2002	<u><u>12,200</u></u>

Warrants

During 2001, 48,000 common shares were issued relating to the exercise of warrants issued in connection with a line of credit granted to the Group in 1999.

Treasury Shares

At December 31, 2002 the Group held 13,500 treasury shares, which were acquired at an average price of CHF 75.41. The Group held no treasury shares at December 31, 2001.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Note 21. Stock-based compensation

Actelion issues stock options to employees, consultants and scientific advisors. In instances where an option is granted to an employee with an exercise price below the market value of the underlying common stock at the date of grant, the difference between the exercise price and the market value is expensed. Options generally vest over a four-year period with 25% of the options becoming exercisable each year. Options generally expire ten years after the grant date. In 2002, the shareholders approved an increase in the total number of authorized shares by 500'000. At December 31, 2002, there were 541,497 shares available for grant of future options.

The following table summarizes activity under stock option plans for the years ended December 31:

	2002		2001	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding, beginning of year	2,323,600	53.92	3,397,112	26.23
Granted	353,936	58.38	594,316	77.63
Forfeited	(97,253)	93.04	(51,728)	86.20
Exercised	(241,699)	10.38	(1,616,100)	3.40
Outstanding, end of year	2,338,584	55.98	2,323,600	53.92
Exercisable, end of year.....	1,081,087		697,986	

The following is a summary of options outstanding and options exercisable at December 31, 2002:

<u>Range of Exercise Prices</u>	Options Outstanding			Options Exercisable	
	Options Outstanding	Weighted Average Remaining Contractual Life in Years	Weighted Average Exercise Price	Options Exercisable	Weighted Average Exercise price
0 - 25.00.....	937,550	6.13	4.93	691,685	3.97
25.01 - 50.00.....	251,500	9.28	46.93	25,702	44.33
50.01 - 75.00.....	654,078	8.47	61.15	156,985	61.46
75.01 - 100.00.....	19,776	9.31	77.17	-	-
100.01 - 125.00.....	114,408	7.42	111.82	57,471	112.15
125.01 - 150.00.....	139,096	7.80	138.18	59,472	138.02
150.01 - 175.00.....	33,728	7.78	163.33	13,866	163.19
175.01 - 225.00.....	188,448	7.88	188.05	75,906	188.10
Total	2,338,584		55.98	1,081,087	

Stock-Based Compensation

In connection with certain stock option grants to employees, the Group recorded stock-based compensation expense of CHF 3,140,628 and CHF 8,460,790 for the years ending December 31, 2002 and 2001, respectively, which is being amortized in accordance with FASB Interpretation No. 28 over the vesting periods of the related options, which is generally four years.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

During the years ended December 31, 2002 and 2001, the Group recorded stock-based compensation of CHF 422,091 and CHF 763,514, respectively, relating to the issuance of restricted shares under an employee stock ownership plan of a majority owned subsidiary. Shares sold out of this employee stock ownership plan are accounted for under APB No. 25 and FASB Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation an interpretation of APB Opinion No. 25."

In connection with stock options granted to consultants, the Group recognized stock-based compensation expense of CHF 549,450 and CHF 526,230 for the years ended December 31, 2002 and 2001, respectively. This expense is recognized in accordance with SFAS No. 123 and EITF Issue No. 96-18 "Accounting for Equity Instruments that are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services". Expense is calculated using the Black-Scholes pricing model, using the assumptions discussed below.

Pro Forma Disclosures

The Group elected to follow APB No. 25 to account for employee stock options. Fair values of awards granted under the stock option plan were estimated at grant or purchase dates using a Black-Scholes option pricing model with the following assumptions:

	Year ended December 31,	
	2002	2001
Expected life in years (from vesting date).....	5 years	5 years
Interest rate.....	2.57%	3.02%
Volatility.....	56%	56%
Expected dividend yield	-	-

	Year ended December 31,	
	2002	2001
Net loss	(52,057)	(122,923)
Stock-based employee compensation cost included in the determination of net loss	3,563	9,224
Stock-based employee compensation cost that would have been included in the determination of net income if the fair value based method had been applied to all awards	(16,777)	(17,578)
Pro forma net loss as if the fair value based method had been applied to all awards	(65,271)	(131,277)
Basic and diluted net loss per share	(2.45)	(5.98)
Pro forma basic and diluted loss per share as if the fair value based method had been applied to all awards	(3.07)	(6.38)

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

The weighted-average grant-date fair values of options granted during the years ended December 31, 2002 and 2001 are as follows:

	2002		2001	
	Number of Shares	Weighted Average Grant Date Fair Values	Number of Shares	Weighted Average Grant Date Fair Values
Options whose exercise price is:				
Equal to the market price of the Group's shares at the grant date.....	7,392	27.07	248,906	29.22
Below the market price of the Group's shares at the grant date.....	214,216	34.70	187,819	28.04
Above the market price of the Group's shares at the grant date.....	132,328	25.73	157,591	59.18
Total.....	353,936	31.19	594,316	36.79

Note 22. Comprehensive loss

SFAS No. 130, "Reporting Comprehensive Income", requires unrealized gains (losses) on the Group's available-for-sale securities, and foreign currency translation adjustments to be included in other comprehensive income.

Information regarding the components of accumulated other comprehensive loss are as follows:

	Unrealized gains/(losses) on securities	Foreign currency translation	Accumulated other comprehensive loss
Balance at December 31, 2001	263	(69)	194
Current year other comprehensive loss...	(263)	(459)	(722)
Balance at December 31, 2002.....	-	(528)	(528)

Note 23. Concentrations

Cash and cash equivalents, marketable securities and accounts receivables are financial instruments, which potentially subject the Group to concentrations of credit risk. The Group has not experienced any significant credit losses and does not generally require collateral on receivables.

For the years ended December 31, 2002 and 2001, three distributors accounted for approximately 72% of total sales. At December 31, 2002 and 2001, CHF 8.8 million and CHF 2.4 million, respectively, of trade accounts receivable related to these distributors. Management believes other distributors could be located which would purchase the Group's products on comparable terms; however, the establishment of new distributor relationships could take several months. The Group performs ongoing credit evaluations of its customers' financial condition and extends credit, generally without collateral. In 2002 and 2001, the Group did not record any significant additions to, or losses against, the allowance for doubtful accounts.

The Group is dependent upon toll manufacturers to manufacture its product. For the years ended December 31, 2002, one supplier accounted for approximately 36% of total purchases while in 2001 another supplier accounted for approximately 44% of total purchases. Management believes other suppliers could provide similar products on comparable terms. A change in suppliers, however, could cause a delay in fulfillment of customer orders and a possible loss of sales, which would adversely affect operating results. Management believes that the Group maintains sufficient inventory levels to minimize the impact a change in suppliers would have on operating results.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Note 24. Executive compensation

Senior executive and board compensation	Year ended	
	December 31,	
	2002	2001
Senior executives		
Monetary compensation	4,197	2,242
Share options granted.....	97,200	52,168
Members	11	9
Board members		
Monetary compensation	105	90
Share options granted.....	13,500	5,000
Members	7	6

Note 25. Subsequent Events

Sale lease back transaction

On September 30, 2003, the Group sold a building to a third party real estate management company. The Group received CHF 14 million of total consideration and used the proceeds to repay the outstanding mortgage on the building. At same time the Group entered into a 10-year lease.

Convertible Bond

In October 2003, the Group issued CHF 143.8 million in convertible bonds. The bonds are convertible into shares of the Group up to October 1, 2008. The bonds carry a zero coupon with a yield to maturity at the time of issuance of 4.75%. Except in the case of redemption after a substantial majority of the bonds have been converted or repurchased, or in the event that the Group becomes required to pay additional tax amounts, the Group may not call the bonds before October 15, 2006. The conversion price of the bonds is CHF 153.40 per share. If all bonds are converted into shares at this conversion price, the Group would issue an additional 937,093 shares, if not converted, the Group would pay a redemption price of 126.12% of the principal amount of the bonds.

Acquisition of Axovan

On October 31, 2003, the Group acquired Axovan Ltd ("Axovan"), a privately-held biopharmaceutical company in Switzerland focused on the research and development of new compounds. The Group acquired all of the remaining common stock of Axovan for CHF 53 million. As part of the acquisition, the Group agreed to pay additional amounts to the shareholders of Axovan based on future product development milestones. The total additional value of these milestone payments is CHF 192 million. The Group cannot estimate when or if these additional milestone payments will be made. The Group acquired Axovan to gain access to Axovan's licenses and to expand Actelion's research capacities.

The acquisition will be accounted for as a purchase and, accordingly, the purchase price will be allocated to the assets acquired and liabilities assumed based on their estimated fair values at the date of the acquisition. The Group estimates that CHF 47 million of the purchase price will be allocated to in-process research and development projects and other intangible assets that have no alternative future use. This allocation represented the estimated fair value based on risk-adjusted cash flows related to the incomplete research and development projects. At the date of the acquisition, development of these projects had not yet reached technological feasibility and the research and development in progress has no alternative future use. Accordingly, these costs were expensed as of the acquisition date.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

In making its preliminary purchase price allocation, the Group considered present value calculations of income, an analysis of project accomplishments and remaining outstanding items, an assessment of overall contributions, as well as technological and regulatory risks. The value assigned to purchased in-process technology was determined by estimating the costs to develop the acquired technology into commercially viable products, estimating the resulting net cash flows from the projects, and discounting the net cash flows to their present value. The revenue projection used to value the in-process research and development was based on estimates of relevant market sizes and growth factors, expected trends in technology, and nature and expected timing of new product introductions by Axovan and its competitors.

The rates utilized to discount the net cash flows to their present value were based on estimated cost of capital calculations. Due to the risks associated with the projected cash flow forecast, a discount rate of 15% percent was considered appropriate for the in-process research and development. The selected rate reflects the inherent uncertainties surrounding the successful development of the purchased in-process technology, the useful life of such technology, and the uncertainty of technological advances that are unknown at this time.

If these projects are not successfully developed, the sales and profitability of the combined companies may be adversely affected in future periods. Additionally, the value of other acquired intangible assets may become impaired. The Group believes that the research and development projects acquired in connection with the acquisition of Axovan are expected to continue in line with the estimates described above.

The following table summarizes the preliminary allocation of the purchase price to the net assets acquired:

Cash and cash equivalents acquired	11,482
Prepaid expenses and other current assets	634
Property, plant and equipment	1,809
In-process research and development.....	46,990
Accounts payable and accrued expenses	(1,451)
Other non current liabilities	(103)
Contingent consideration.....	<u>(6,641)</u>
Total fair value of net assets acquired.....	<u>52,720</u>

The final determination of the purchase price allocation will be based on the fair values of assets acquired, including the fair values of in-process research and development and other identifiable intangibles, and the fair values of liabilities assumed as of the date that the acquisition is consummated. The purchase price allocation will remain preliminary until the Group completes a third-party valuation of significant identifiable intangible assets acquired (including in-process research and development) and determines the fair values of other assets and liabilities acquired. The final determination of the purchase price allocation is expected to be completed as soon as practicable after the consummation of the acquisition.

Merck Collaboration

In December 2003, the Group and Merck & Co., Inc. (“Merck”), formed an exclusive worldwide alliance to discover, develop and market new classes of renin inhibitors. This alliance will enable the Group and Merck to combine their discovery, development and marketing capabilities with the goal to efficiently provide innovative and better medicines to patients suffering from cardio-renal diseases. Development funding will be initially shared by both parties, with Merck fully responsible to fund pivotal Phase III and outcome studies. Merck will lead and fund commercialization. The Group retains a worldwide option to co-promote any product resulting from this alliance as a paid-for sales force. Merck will pay the Group an upfront payment of USD 10 million. In addition, the Group will be eligible to receive additional payments of up to USD 262 million for the successful commercialization of the first collaboration product. The Group will also be eligible to receive certain milestone payments for the successful commercialization of additional products. Merck will pay the Group substantial royalties on the sale of all products resulting from this alliance.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(CHF thousands, except share and per share amounts)

Sale of Hesperion

During 2003, management formally committed to a plan to sell its share in Hesperion AG ("Hesperion"). Subsequently the Group identified a potential buyers and in December 2003 signed a letter of intent with Cerep SA ("Cerep"). On January 14, 2004, the Group, other shareholders and Cerep signed a share purchase agreement. The total sale price for Hesperion is estimated to be CHF 16.1 million. Hesperion was originally acquired by the Group in 1999 to enable Actelion to rapidly expand its capacity to conduct clinical trials. With the growth of both the Group and Hesperion it is now not necessary for Actelion to have an "in-house" CRO. The sale will enable the Group to concentrate on its core business of the discovery, development and marketing of innovative medical products in areas where there exists a high level of unmet medical need.