

ACTELION LTD AND SUBSIDIARIES
INDEX TO THE CONSOLIDATED FINANCIAL STATEMENTS

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Report of the group auditors
to the general meeting 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, 2003 and 2002, the consolidated statements of operations, of cash flows, of changes in shareholders' equity for the years ended December 31, 2003 and 2002 and the notes to the consolidated financial statements as presented on pages 3 to 31.

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 present fairly, in all material respects, the financial position of Actelion Ltd and its subsidiaries at December 31, 2003 and 2002 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.

PricewaterhouseCoopers AG

Thomas Brüderlin Hans-Rudolf Tanner

Basel, February 27, 2004

ACTELION LTD AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

<i>(in CHF thousands, except share and per share amounts)</i>	Note	For the year ended December 31,	
		2003	2002
Net revenue:			
Products sales.....	2	300,315	121,834
Contract revenue.....	2	7,229	10,614
Total net revenue.....		307,544	132,448
Operating expenses			
Cost of sales.....		31,816	13,076
Research and development.....		79,173	50,632
Marketing and advertising.....		79,828	56,584
Selling, general and administration.....		69,645	42,974
Amortization of acquired intangible assets.....	13	1,756	1,221
Write-off of acquired in -process research and development.....	3	46,990	-
Total operating expense.....		309,208	164,487
Operating loss.....		(1,664)	(32,039)
Interest income.....		946	1,700
Interest expense.....		(885)	(346)
Amortization of debt discount and issuance costs		(1,500)	-
Other financial income (expense), net.....		2,567	(5,682)
Loss from continuing operations before income tax expense and share in loss of affiliate.....		(536)	(36,367)
Income tax expense.....	7	(830)	(113)
Loss from continuing operations before share in loss of affiliate.....		(1,366)	(36,480)
Share in loss of affiliate.....	3	(1,089)	(1,092)
Loss from continuing operations.....		(2,455)	(37,572)
Loss from discontinued operations, net of tax and minority interest.....	4	(7,461)	(14,485)
Net loss.....		(9,916)	(52,057)
Basic and diluted loss per share			
Continuing Operations.....	8	(0.11)	(1.77)
Discontinued Operations.....		(0.35)	(0.68)
Net loss.....		(0.46)	(2.45)

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,	
		2003	2002
Assets			
Current assets			
Cash and cash equivalents.....	9	258,770	116,201
Marketable securities	10	-	4,851
Derivative instruments	10	2,199	1,622
Trade and other receivables, net	11	66,711	21,743
Inventories.....	12	21,455	13,821
Other current assets.....		3,966	2,841
Current assets of discontinued operations.....	4	10,385	3,460
Total current assets.....		363,486	164,539
Marketable securities, long-term.....	10	-	6,898
Property, plant and equipment, net.....	14	18,982	15,079
Investment in affiliate.....	3	-	2,171
Other assets.....		6,687	3,168
Intangible assets, net	13	8,813	9,945
Goodwill, net	13	3,784	3,672
Non-current assets of discontinued operations.....	4	1,091	13,488
Total assets.....		402,843	218,960
Liabilities and Shareholders' Equity			
Current liabilities			
Trade and other payables.....		27,535	25,108
Accrued expenses.....	15	37,601	18,549
Deferred revenue, less current portion.....	6	10,821	6,318
Financial debt.....	16	41,161	-
Other current liabilities.....	17	2,019	563
Contingent consideration.....	3	6,641	-
Current liabilities of discontinued operations.....	4	8,758	5,373
Total current liabilities.....		134,536	55,911
Long-term financial debt, less current portion	16	145,147	40,000
Deferred revenue, less current portion.....	6	64,468	62,712
Other non-current liabilities.....	18	1,963	2,052
Non-current liabilities of discontinued operations.....	4	1,785	7,471
Total liabilities.....		347,899	168,146
Minority interest of discontinued operations.....	4	517	494
Commitments and contingencies.....	17		
Shareholders' Equity			
Common shares (par value CHF2.50 per share, authorized 30,506,640 and 27,456,640 shares; issued 21,751,148 and 21,376,559 shares in 2003 and 2002, respectively).....		54,378	53,441
Additional paid-in-capital.....		302,817	289,671
Accumulated deficit		(297,226)	(287,310)
Unearned compensation.....		(5,369)	(3,936)
Treasury shares, at cost.....	19	(1,018)	(1,018)
Accumulated other comprehensive income (loss)	21	845	(528)
Total shareholders' equity.....		54,427	50,320
Total liabilities, minority interest and shareholders' equity.....		402,843	218,960

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,	
	2003	2002
<i>(in CHF thousands)</i>		
Cash flows from operating activities		
Net loss.....	(9,916)	(52,057)
Loss from discontinued operations, net of minority interest.....	7,461	14,485
Loss from continuing operations	(2,455)	(37,572)
Adjustments to reconcile net loss to net cash provided from operating activities:		
Depreciation and amortization.....	7,549	5,301
Share in loss of affiliate.....	1,089	1,092
Stock-based compensation.....	4,819	3,690
Realized (gain) loss on sale of marketable securities.....	(602)	1,101
Gain on derivative instruments.....	(937)	(924)
Write-off of acquired in-process research and development.....	46,990	-
Amortization of debt discount and issuance costs.....	1,500	-
Increase in trade and other receivables.....	(44,837)	(13,880)
Increase in inventories.....	(7,633)	(7,575)
Increase in other current assets.....	(951)	(905)
Increase in other assets.....	(461)	(1,212)
Increase in trade and other payables.....	8,592	9,382
Increase in accrued expenses.....	18,290	13,088
Increase (decrease) in deferred revenue.....	5,891	(7,632)
Increase in other liabilities.....	1,484	265
Net cash flow provided by (used in) operating activities	38,328	(35,781)
Cash flows from investing activities		
Purchase of marketable securities.....	-	(13,235)
Proceeds from sale of marketable securities.....	12,794	58,571
Purchase of property, plant and equipment.....	(7,114)	(5,351)
Purchase of derivative instruments.....	(1,621)	-
Proceeds from sale of derivative instruments.....	1,477	-
Purchase of intangible assets.....	(7,101)	(599)
Increase in investment in affiliate.....	-	(505)
Acquisition of subsidiary.....	(40,148)	-
Net cash flow provided by (used in) investing activities	(41,713)	38,881
Cash flows from financing activities		
Payments on capital leases.....	(607)	(713)
Proceeds from issuance of financial debt.....	141,677	40,000
Proceeds from exercise of stock options.....	7,553	1,215
Acquisition of treasury shares.....	-	(1,018)
Proceeds from sale of treasury shares.....	-	55
Net cash flow provided by financing activities	148,623	39,539
Net effect of exchange rates on cash and cash equivalents.....	(993)	670
Net effect of discontinued operations.....	(1,676)	(18,141)
Net change in cash and cash equivalents	142,569	25,168
Cash and cash equivalents at beginning of year.....	116,201	91,033
Cash and cash equivalents at end of year.....	258,770	116,201
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest.....	972	162
Taxes.....	168	283

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, 2002	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 income (loss):								
Unrealized gain (loss) on marketable securities.....							(263)	(263)
Currency translation adjustment.....							(459)	(459)
Comprehensive loss								(52,779)
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
Comprehensive loss net of tax effect:								
Net loss				(9,916)				(9,916)
Other comprehensive income (loss):.....								
Currency translation adjustment.....							1,373	1,373
Comprehensive loss								(8,543)
Changes in underlying equity of affiliate.....			93					93
Exercise of stock options.....	374,589	937	6,616					7,553
Stock-based compensation expense, net			653		4,351			5,004
Issuance of stock options.....			6,023		(6,023)			-
Stock option forfeitures and cancellations.....			(239)		239			-
At December 31, 2003	21,737,648	54,378	302,817	(297,226)	(5,369)	(1,018)	845	54,427

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
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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 and milestone payments associated with collaborations with third parties. 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 5, "Licensing Agreements."

Advertising costs

The Group expenses the costs of advertising, including promotional expenses, as incurred. Advertising expenses were CHF 37.0 million in 2003 and CHF 28.0 million in 2002.

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
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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.

Earnings per share

Basic earnings per share is computed using the weighted average number of common shares outstanding during the period. Diluted earnings 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
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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 income (expense) in the consolidated statements of operations. See Note 10, "Investments" 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. See Note 10, "Investments" 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 might 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 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 a gain to the Group's additional paid-in-capital.

ACTELION LTD AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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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.....	5 to 10 years

The carrying values of the Group's long-lived assets are 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 the fair value of net assets acquired in a business combination. Pursuant to SFAS 142, "Goodwill and Other Intangibles", goodwill is not amortized and is regularly reviewed for impairment.

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
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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, 2003 and 2002 has been reflected in the consolidated statement of changes in shareholders' equity.

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 "currency 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 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 apply to revenue arrangements entered into in fiscal periods beginning after June 15, 2003. EITF 00-21 did not have a material impact on adoption.

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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 structure 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. FIN 46 is effective for the Group starting January 1, 2004. The Group has not identified any variable interest entities, therefore, the adoption of FIN 46 is not expect to have a material 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 did not have a material effect on the Group's results of operations, cash flows or financial position.

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. EITF Issue 01-08 did not have a material impact on adoption.

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 did not have a material impact on adoption.

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 aggregated basis and manage the operations of the Group as a single operating segment. The Group currently derives product revenue from sales of Tracleer for the treatment of pulmonary arterial hypertension and Zavesca for the treatment of Type I Gaucher's disease. 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.

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The Group's geographic information is as follows:

December 31, 2003:	Switzerland	United States	Europe	Other	Total
Product revenue from external customers.....	6,763	160,760	122,988	9,804	300,315
Contract revenue from external customers	7,229	-	-	-	7,229
Long-lived assets.....	24,476	1,130	3,812	2,161	31,579
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	10,614	-	-	-	10,614
Long-lived assets.....	22,978	1,084	3,494	1,141	28,697

Note 3. 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 could total CHF 192 million and would be treated as goodwill. The Group acquired Axovan to gain access to Axovan's licenses and to expand Actelion's research capacities.

The acquisition has been accounted for as a purchase and, accordingly, the purchase price has been allocated to the assets acquired and liabilities assumed based on their estimated fair values at the date of the acquisition. The Group has allocated CHF 47 million of the purchase price to in-process research and development projects and other intangible assets with 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.

In making its 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.

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The following table summarizes the 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	(6,641)
Total fair value of net assets acquired	<u>52,720</u>

The movements in the Group's investment in Axovan until it was consolidated as of October 31, 2003 consisted of the following:

	October 31, 2003	December 31, 2002
Investment at January 1,	2,171	815
Additional investment	-	505
Share in loss	(1,089)	(1,092)
Increase in underlying equity	93	1,943
Investment at	<u>1,175</u>	<u>2,171</u>
Ownership percentage at end of period	8.7%	8.7%

Note 4. Sale of Hesperion

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. This transaction resulted in an increase in the Group's share of Hesperion to 74%. The Group increased its interest to maintain a controlling interest and to further capitalize Hesperion. The fair value of the net assets acquired was not materially different from the carrying values of those assets. As a result, the entire purchase price of CHF 520,039 was allocated to goodwill. Minority interests at December 31, 2003 and 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, 2002:

	2003	2002
January 1	494	1,184
Change in minority interest due to capital transaction	-	602
Change in minority interest due to result of the year	24	(1,286)
Change in translation adjustment	(1)	(6)
December 31	<u>517</u>	<u>494</u>

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During 2003, management formally committed to a plan to sell its 74% share in Hesperion and began the process of identifying a potential buyer. On January 14, 2004, the Group entered into a contract to sell its shareholding in Hesperion AG ("Hesperion") to Cerep SA. The total sales 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. Accordingly, the financial statements as of and for the years ended December 31, 2003 and 2002 reflect Hesperion as a discontinued operation.

For the years ended December 31, 2003 and 2002, Hesperion had revenues of CHF 10.6 million and CHF 7.8 million, net losses of CHF 7.5 million and CHF 14.1 million, and tax expenses of CHF 0.04 million and CHF 0.2 million, respectively.

Note 5. 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 2003 and 2002.

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, 2003 and 2002, payments of CHF 9 million are included in intangible assets and are amortized over 11 years. 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.

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 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 is the Group's sole supplier of Zavesca.

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Note 6. 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 year ended December 31, 2002 the Group recognized revenue of CHF 3.9 million. In October 2003, the agreement was amended to the effect that the Group would be the best placed to continue development of the compounds covered by the collaboration. The Group therefore, has now sole rights for the ongoing development and potential commercialization of these compounds. If successful, the Group will pay J&J a small royalty on sales generated from these compounds.

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, 2003 and 2002 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 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, 2003 and 2002, the Group recognized revenue of CHF 4.9 million and CHF 4.9 million respectively, under this agreement.

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 enables 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 made 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. For the year ended December 31, 2003, the Group recognized revenue of CHF 0.3 million under this agreement.

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Note 7. Income taxes

The following table sets forth the components of income tax expense:

	For the Year Ended December 31,	
	2003	2002
Current tax expense:		
Switzerland	105	
Foreign	725	113
Total current tax expense	830	113

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

	For the Year Ended December 31,	
	2003	2002
Switzerland	(19,287)	6,456
Foreign	19,823	30,335
Total	536	36,791

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 2003 and 2002 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, 2003 and 2002 are shown below. A valuation allowance of CHF 42.6 million (2002: CHF 48.3 million), has been recognized because of the Group's historical cumulative operating losses. The Group has CHF 155.4 million of tax loss carryforwards, which expire between 3 and 5 years.

	2003	2002
Deferred tax assets:		
Net benefit from operating loss carryforwards.....	29,909	35,866
Deferred revenue	6,927	10,700
Other	5,794	1,767
Total deferred tax assets	42,630	48,333
Valuation allowance for deferred tax assets	(42,630)	(48,333)
Net deferred tax assets	-	-

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Note 8. Loss Per Share

For the years ended December 31, 2003, and 2002, loss per basic and diluted share are based on weighted average common shares and exclude diluted shares of 1'100'407 and 951'590, respectively, relating to employee stock options, as they would be anti-dilutive due to the reported losses.

	<u>2003</u>	<u>2002</u>
Loss on continuing operations.....	(2,455)	(37,572)
Loss on discontinued operations.....	(7,461)	(14,485)
Net loss.....	(9,916)	(52,057)
Weighted average number of shares outstanding.....	21,567,195	21,282,433
Basic and diluted loss per share of continuing operations.....	(0.11)	(1.77)
Basic and diluted loss per share of discontinued operations...	(0.35)	(0.68)
Basic and diluted loss per share of net loss.....	(0.46)	(2.45)

Note 9. Cash and cash equivalents

Cash and cash equivalents consisted of the following at December 31, 2003 and 2002:

	<u>2003</u>	<u>2002</u>
Cash.....	154,385	45,960
Short-term bank deposits.....	102,932	69,665
Money market funds.....	1,453	576
Total	<u><u>258,770</u></u>	<u><u>116,201</u></u>

Note 10. Investments

Marketable Securities

During September 2003, management changed its investment strategy and decided to sell investments of CHF 11.8 million previously classified as held-to-maturity for a realized gain of CHF 409,676. In accordance with US GAAP, as a result of selling these investments prior to their maturity, the Group is precluded from classifying any security as held-to-maturity until 2006. At December 31, 2003 the Group maintained no investments in marketable securities.

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In 2002, realized gains and losses on available-for-sale securities and 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:

	Gains and losses realized in the consolidated statement of operations		Amounts reclassified from accumulated other comprehensive income to the consolidated statement of operations	
	Gains	Losses	Gains	Losses
Available-for-sale securities:				
Short-term equity securities	639	(2,940)	363	(1,171)
Long-term debt securities	1,589	(389)	1,425	(354)
Total Available-for-Sale Securities	2,228	(3,329)	1,788	(1,525)

Financial Instruments

The following tables show the contract or underlying principal amounts and fair values of derivative financial instruments at December 31, 2003 and 2002. 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, 2003 and 2002, respectively.

<u>Derivative financial instruments</u>	<u>Contract or underlying principal amount</u>	<u>Positive fair values</u>	<u>Negative fair values</u>
2002			
Forward foreign exchange rate contracts.....	88,130	1,180	64
Embedded interest rate derivatives		442	
Total	88,130	1,622	64
2003			
Forward foreign exchange rate contracts.....	60,314	2,199	2
Total	60,314	2,199	2

The Group sold in September 2003 their held-to-maturity bonds, which contained embedded derivatives. Changes in the fair value of these derivatives are recognized in earnings, as they do not meet the definition of a hedge. The Group held no such embedded derivatives at December 31, 2003.

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Note 11. Trade and Other Receivables

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

	<u>2003</u>	<u>2002</u>
Trade receivables	62,594	19,279
Other receivables	4,117	2,464
Total	<u>66,711</u>	<u>21,743</u>

Note 12. Inventories

Inventories consisted of the following at December 31:

	<u>2003</u>	<u>2002</u>
Intermediaries	18,331	9,667
Finished products	3,124	4,154
Total	<u>21,455</u>	<u>13,821</u>

Note 13. Goodwill And Other Intangible Assets

Changes in the net carrying amount of goodwill in 2003 are as follows:

<u>Balance at January 1</u>	<u>Translation effects</u>	<u>Additions</u>	<u>Balance at December 31</u>
3,672	112	-	3,784

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

	<u>2003</u>			<u>2002</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	(1,383)	7,617	9,000	(506)	8,494
Acquired software and other	3,046	(1,850)	1,196	2,487	(1,036)	1,451
Total	<u>12,046</u>	<u>(3,233)</u>	<u>8,813</u>	<u>11,487</u>	<u>(1,542)</u>	<u>9,945</u>

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Amortization expense of other intangible assets are as follows:

	<u>2003</u>	<u>2002</u>
Other intangible assets amortization.....	1,756	1,221
Total amortization expense.....	<u>1,756</u>	<u>1,221</u>

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

For the year ending December 31,	<u>Amortization Expense</u>
2004	1,611
2005	1,227
2006	991
2007	877
2008	877
Thereafter.....	3,230
Total expected future amortization	<u>8,813</u>

Note 14. Property, plant and equipment

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

	<u>2003</u>	<u>2002</u>
At cost:		
Furniture and fixtures and lab equipment.....	28,554	20,144
Computers	5,910	4,023
Other tangible assets	1,456	549
Less: accumulated depreciation and amortization	(16,938)	(9,637)
Property, plant and equipment, net	<u>18,982</u>	<u>15,079</u>

Depreciation expense was CHF 5.8 million in 2003 and CHF 4.1 million in 2002.

Note 15. Accrued Expenses

Accrued expenses consisted of the following at December 31:

	<u>2003</u>	<u>2002</u>
Personnel and compensation costs	17,908	6,739
Marketing and royalties	2,980	5,767
Research and development expense.....	9,279	3,483
Other accrued expenses	7,434	2,560
Total	<u>37,601</u>	<u>18,549</u>

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Note 16. Borrowings

	2003		2002	
	Total	Due within one year	Total	Due within one year
Convertible bond	145,147	-	-	-
Borrowings from banks	41,161	41,161	40,000	-
Total	186,308	41,161	40,000	-

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, 2003. 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, 2003 approximates the carrying value.

At December 31, 2003, the Group had used credit lines of CHF 1.2 million with interest rates on an average of 1.875% on the outstanding balance.

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. The fair value of the convertible bond at December 31, 2003 is 118.8% of the principal amount (CHF 170.8 million). Debt issuance costs amounted to CHF 3.2 million and were recorded in other non current assets.

At December 31, 2003 the aggregate amounts of indebtedness maturing during the next five years and thereafter are as follows:

Year ending December 31,	<u>Debt Financings</u>
2004.....	41,161
2005.....	-
2006.....	-
2007.....	-
2008.....	181,298
Thereafter.....	-
Total	222,459

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Note 17. Lease Commitments

Capital Leases

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

	<u>2003</u>	<u>2002</u>
Laboratory equipment.....	4,212	4,239
Computers and software	439	283
Other tangible assets	180	32
Less: accumulated depreciation and amortization	(3,845)	(2,986)
Net assets leased under capital leases.....	<u>986</u>	<u>1,568</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 2004 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 non-cancelable operating and capital leases at December 31, 2003 are as follows:

Year ended December 31,	<u>Operating Leases</u>	<u>Capital Leases</u>
2004.....	6,312	142
2005.....	7,450	101
2006.....	12,894	82
2007.....	11,979	62
2008.....	11,391	33
Thereafter	85,845	-
Total minimum payments	<u>135,871</u>	<u>420</u>
Less amounts representing interest.....		(59)
Present value of future debt payments		<u>361</u>
Less current portion of debt.....		124
Non-current portion of debt		<u>237</u>

Rent expense under operating leases was CHF 9.6 million and CHF 6.2 million for the years ended December 31, 2003 and 2002, respectively.

In October 2003, the Group signed a lease agreement for a new building to be constructed over the next 2 years. The agreement contains a committed lease period of 15 years with an option to extend for another 10 years or an option to buy the building at market rates after the first lease period of 10 years has ended. Future payments under this lease agreement amounts to a yearly lease expense of an estimated CHF 6.5 million, which are included in the table above.

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Note 18. Retirement Plans

The Group has entered into a term agreement with a third party insurance company to minimize the risk associated with a pension obligation. For accounting purposes this insurance contract represents the sole asset of the Plan. This investment strategy was adopted as a means to reduce the uncertainty and volatility of the Plan's assets for the Group. Fair value of plan assets is the estimated cash surrender value at the respective balance sheet date.

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 2003 and 2002 include the following components:

	<u>2003</u>	<u>2002</u>
Service cost.....	2,287	2,025
Interest cost.....	804	689
Expected return on plan assets.....	(704)	(591)
Amortization of net transition amount.....	80	79
Net periodic pension cost.....	<u>2,467</u>	<u>2,202</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>2003</u>	<u>2002</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%

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The following tables set forth the change in benefit obligations and change in plan assets at December 31, 2003 and 2002 for the Group's defined benefit plans:

	<u>2003</u>	<u>2002</u>
Change in Projected Benefit Obligation		
Projected benefit obligation – beginning of year	18,287	16,395
Change in projected benefit obligation (acquisition)	3,296	
Service cost.....	2,287	2,025
Interest cost.....	804	689
Plan participant contributions.....	1,846	1,280
Actuarial loss.....	(397)	(332)
Transfers in	5,187	1,463
Transfers out.....	(696)	(3,233)
Projected Benefit obligation – end of year	<u>30,614</u>	<u>18,287</u>
Change in Plan Assets		
Plan assets at fair value – beginning of year	17,129	14,773
Change in plan assets at fair value (acquisition)	2,864	
Actual return on plan assets	(454)	920
Group contributions.....	2,714	1,926
Plan participant contributions.....	1,846	1,280
Transfers in	5,187	1,463
Transfers out.....	(696)	(3,233)
Plan assets at fair value – end of year	<u>28,590</u>	<u>17,129</u>

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

	<u>2003</u>	<u>2002</u>
Plan assets less than projected benefit obligation	(2,024)	(1,158)
Unrecognized actuarial losses/(gains).....	1,197	118
Unrecognized net transition asset.....	-	79
Total recognized in the consolidated balance sheet.....	<u>(827)</u>	<u>(961)</u>

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

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

	<u>2003</u>	<u>2002</u>
Accumulated benefit obligation	28,479	16,992
Projected benefit obligation	30,614	18,287
Plan assets at fair value	28,590	17,129

Certain of the Group's subsidiaries sponsor defined contribution plans. Total contribution expense to these plans in 2003 and 2002 was CHF 1,621,670 and CHF 983,255, respectively. The contribution payable at December 31, 2003 and 2002, was CHF 105,916 and CHF 277,755, respectively.

Note 19. Shareholders' Equity

Authorized Capital

The Annual General Meeting of April 23, 2003 authorized an increase in share capital to be used for strategic purposes. The Board of Directors is authorized to increase until April 23, 2005 the share capital to an amount of not more than CHF 10 million by issuance of not more than 4 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 and convertible bonds as well as for the potential issuance of shares in relation with certain credit facilities. At December 31, 2003, the Group has conditional capital of CHF 11.9 million.

Movements in conditional capital are as follows:

January 1, 2002	9,434
Creation of conditional capital for employee stock option plans	1,250
Creation of conditional capital for convertible bonds/loans	2,120
Exercise of options.....	(604)
December 31, 2002	<u>12,200</u>
Creation of conditional capital for employee stock option plans.....	625
Exercise of options.....	(937)
December 31, 2003	<u>11,888</u>

Treasury Shares

At December 31, 2003 the Group held 13,500 treasury shares, which were acquired at an average price of CHF 75.41.

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Note 20. 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. One option is entitled to one share.

In April 2003, Actelion created a Directors' Share Option Plan with immediate vesting of options.

Options generally expire ten years after the grant date. In 2003, the shareholders approved an increase in the total number of authorized shares by 250'000. At December 31, 2003, there were 127,923 shares available for grant of future options.

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

	2003		2002	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding, beginning of year	2,338,584	55.98	2,323,600	53.92
Granted	744,432	77.37	353,936	58.38
Forfeited	(80,858)	90.16	(97,253)	93.04
Exercised	(374,589)	20.16	(241,699)	10.38
Outstanding, end of year	2,627,569	64.63	2,338,584	55.98
Exercisable, end of year	1,153,699		1,081,087	

The following is a summary of options outstanding and options exercisable at December 31, 2003:

<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	682,090	5.08	4.70	642,610	4.33
25.01 - 50.00	226,001	8.33	47.23	46,800	46.24
50.01 - 75.00	982,637	8.24	61.63	203,440	61.56
75.01 - 100.00	223,669	9.51	92.16	4,365	77.29
100.01 - 125.00	192,996	7.81	112.00	79,860	112.42
125.01 - 150.00	121,520	7.07	136.44	60,618	137.65
150.01 - 175.00	31,808	6.75	163.22	18,537	163.12
175.01 - 225.00	166,848	6.84	188.13	97,469	188.24
Total	2,627,569		64.63	1,153,699	48.97

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Stock-Based Compensation

In connection with certain stock option grants to employees, the Group recorded stock-based compensation expense of CHF 4,350,270 and CHF 3,140,628 for the years ending December 31, 2003 and 2002, 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.

In connection with stock options granted to consultants, the Group recognized stock-based compensation expense of CHF 468,198 and CHF 549,450 for the years ended December 31, 2003 and 2002, 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 and 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,	
	2003	2002
Expected life in years (from vesting date).....	5 years	5 years
Interest rate.....	3.02%	2.57%
Volatility.....	56%	56%
Expected dividend yield	-	-

	Year ended December 31,	
	2003	2002
Net loss from continuing operations.....	(2,455)	(37,572)
Stock-based employee compensation cost included in the determination of net loss from continuing operations.....	4,350	3,141
Stock-based employee compensation cost that would have been included in the determination of net loss from continuing operations if the fair value based method had been applied to all awards	(22,278)	(16,440)
Pro forma net loss from continuing operations as if the fair value based method had been applied to all awards	(20,383)	(50,871)
Basic and diluted net loss per share of continuing operations	(0.11)	(1.77)
Pro forma basic and diluted loss per share from continuing operations as if the fair value based method had been applied to all awards.....	(0.95)	(2.39)

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The weighted-average grant-date fair values of options granted during the years ended December 31, 2003 and 2002 are as follows:

	2003		2002	
	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.....	3,166	31.06	7,392	27.07
Below the market price of the Group's shares at the grant date.....	532,830	48.31	214,216	34.70
Above the market price of the Group's shares at the grant date.....	208,436	34.17	132,328	25.73
Total.....	<u>744,432</u>	<u>44.28</u>	<u>353,936</u>	<u>31.19</u>

Note 21. Comprehensive income (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.

As of December 31, 2003 and 2002 the accumulated other comprehensive income (loss) consists of foreign currency translation of CHF 0.8 million and CHF (0.5) million, respectively.

Note 22. 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, 2003 and 2002, three distributors accounted for approximately 54% and 72%, respectively of total sales. At December 31, 2003 and 2002, CHF 18.0 million and CHF 8.8 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 2003 and 2002, 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, 2003, one supplier accounted for approximately 60% of total purchases while in 2002 another supplier accounted for approximately 36% 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.

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Note 23. Executive compensation

Senior executive and board compensation	Year ended	
	December 31,	
	2003	2002
Senior executives		
Monetary compensation	4,694	4,197
Share options granted.....	53,600	97,200
Bonus shares granted	600	-
Members.....	11	11
Board members		
Monetary compensation	110	105
Share options granted.....	5,000	13,500
Bonus shares granted	1,650	-
Members.....	5	7

Note 24 Related Party Transactions

Amongst the former shareholders of Axovan were two board members of Actelion and a company related to a third board member. They sold their interest in Axovan on the same commercial terms and conditions as those offered to the other shareholders of Axovan. The total cash consideration paid in this respect amounted to CHF 17.4 million.

A member of the board of Actelion provided consultation services to the Company in exchange for fees of CHF 35,847.

Note 25. Subsequent Events

On 9th February 2004, the sale of Hesperion to Cerep SA was successfully completed at a total sales price of CHF 16.1 million.