VERTEX PHARMACEUTICALS INC / MA
Form 10-Q
August 14, 2002

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(MARK ONE)

/X/ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES AND EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2002
OR

/ / TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES AND EXCHANGE ACT OF 1934

FOR THE TRANSITION PERIOD FROM _____ TO _____

COMMISSION FILE NUMBER 000-19319

VERTEX PHARMACEUTICALS INCORPORATED

(Exact name of registrant as specified in its charter)

MASSACHUSETTS (State or other jurisdiction of incorporation or organization)	04-3039129 (I.R.S. Employer Identification No.)
130 WAVERLY STREET, CAMBRIDGE, MASSACHUSETTS (Address of principal executive offices, including zip code)	02139-4242 (zip code)

(617) 444-6100
(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports

required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES /X/ NO / /

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at August 12, 2002
Common Stock, par value $.01 per share	76,022,827

VERTEX PHARMACEUTICALS INCORPORATED

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VERTEX PHARMACEUTICALS INCORPORATED

CONDENSED CONSOLIDATED BALANCE SHEETS

	JUNE 30, 2002	DECEMBER 31, 2001
	(UNAUDITED)	
	(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 125,268	$ 189,205
Marketable securities, available for sale	554,577	553,997
Accounts receivable	18,056	20,265
Prepaid expenses	4,548	6,636
Other current assets	5,159	5,989
Total current assets	707,608	776,092
Restricted cash	26,125	26,190
Property and equipment, net	86,222	80,377
Investments	26,433	26,433
Other assets	14,086	16,039
Total assets	$ 860,474	$ 925,131
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 9,764	$ 11,628
Accrued expenses and other current liabilities	22,764	31,381
Accrued interest	4,464	4,467
Deferred revenue	21,775	39,498
Obligations under capital leases and other obligations	3,519	4,579
Total current liabilities	62,286	91,553
Obligations under capital leases and other obligations, excluding current portion	6,730	8,026
Deferred revenue, excluding current portion	39,778	35,201
Convertible subordinated notes (due September 2007)	315,000	315,000
Total liabilities	423,794	449,780
Stockholders' equity:		
Preferred stock, $0.01 par value; 1,000,000 shares authorized; none issued and outstanding	--	--
Common stock, $0.01 par value; 200,000,000 shares authorized; 75,771,504 and 75,055,160 shares issued and outstanding at June 30, 2002 and December 31, 2001, respectively	758	751
Additional paid-in capital	786,886	778,018
Deferred compensation, net	--	(20)
Accumulated other comprehensive income	6,654	11,134
Accumulated deficit	(357,618)	(314,532)
Total stockholders' equity	436,680	475,351
Total liabilities and stockholders' equity	$ 860,474	$ 925,131

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

VERTEX PHARMACEUTICALS INCORPORATED

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2002	2001*	2002	2001*
	(UNAUDITED) (IN THOUSANDS, EXCEPT PER SHARE DATA)			
Pharmaceutical revenues:				
Royalties	$ 2,384	$ 2,862	$ 4,858	$ 5,458
Collaborative research and development revenues	18,859	16,273	36,936	31,846
Discovery tools and service revenues:				
Product sales and royalties	15,587	15,423	30,797	26,952
Service revenues	5,500	6,083	10,434	11,341
Total revenues	42,330	40,641	83,025	75,597
Costs and expenses:				
Royalty payments	828	972	1,645	1,853
Cost of product sales and royalties	2,662	6,828	7,252	13,696
Cost of service revenues	2,972	2,396	6,206	5,186
Research and development	46,546	34,577	93,568	67,117
Sales, general and administrative	13,348	11,380	24,443	22,329
Merger related costs	--	4,363	--	5,542
Total costs and expenses	66,356	60,516	133,114	115,723
Loss from operations	(24,026)	(19,875)	(50,089)	(40,126)
Interest income	7,467	11,768	15,925	24,838
Interest and other expense, net	(4,460)	(5,271)	(8,922)	(10,304)
Loss before cumulative effect of change in accounting principle	(21,019)	(13,378)	(43,086)	(25,592)
Cumulative effect of change in accounting principle	--	--	--	(25,901)
Net loss	$(21,019)	$(13,378)	$(43,086)	$(51,493)
Basic and diluted loss per common share before cumulative effect of change in accounting principle	$ (0.28)	$ (0.18)	$ (0.57)	$ (0.34)
Basic and diluted cumulative effect of change in accounting principle	--	--	--	(0.35)
Basic and diluted net loss per common share	$ (0.28)	($ 0.18)	$ (0.57)	($ 0.69)
Basic and diluted weighted average number of common shares outstanding	75,660	74,381	75,408	74,152

* Results have been adjusted to reflect the adoption of the Substantive Milestone method of revenue recognition in the third quarter of 2001, retroactive to January 1, 2001. See Note 3, "Change in Accounting Principle--Revenue Recognition," for more information.

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

VERTEX PHARMACEUTICALS INCORPORATED

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	SIX MONTHS ENDED JUNE 30,	
	2002	2001
	(UNAUDITED) (IN THOUSANDS)	
Cash flows from operating activities:		
Net loss	$(43,086)	$(51,493)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	11,563	7,488
Other non-cash items, net	1,439	1,080
Realized (gains)/losses on marketable securities	(1,016)	(326)
Cumulative effect of change in accounting principle	--	25,901
Changes in operating assets and liabilities:		
Accounts receivable	2,210	880
Prepaid expenses	2,089	97
Other current assets	1,155	(1,878)
Accounts payable	(1,864)	2,429
Accrued expenses and other current liabilities	(7,121)	559
Deferred revenue	(13,146)	(393)
Net cash used in operating activities	(47,777)	(15,656)
Cash flows from investing activities:		
Purchase of marketable securities	(476,363)	(575,899)
Sales and maturities of marketable securities	472,057	454,349
Expenditures for property and equipment	(18,258)	(28,998)
Restricted cash and other assets	(219)	(15,628)
Net cash used in investing activities	(22,783)	(166,176)
Cash flows from financing activities:		
Issuances of common stock, net	8,717	13,793
Principal payments on notes payable, capital leases and other obligations	(2,356)	(2,362)
Net cash provided by financing activities	6,361	11,431
Effect of changes in exchange rates on cash	262	(436)

Net decrease in cash and cash equivalents.....	(63,937)	(170,837)
Cash and cash equivalents--beginning of period.....	189,205	346,659
Cash and cash equivalents--end of period.....	$125,268	$175,822

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

VERTEX PHARMACEUTICALS INCORPORATED

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The accompanying condensed consolidated financial statements are unaudited and have been prepared by Vertex Pharmaceuticals Incorporated ("Vertex" or the "Company") in accordance with generally accepted accounting principles.

The condensed consolidated financial statements reflect the operations of the Company and its wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated.

Certain information and footnote disclosures normally included in the Company's annual financial statements have been condensed or omitted. Certain prior year amounts have been reclassified to conform with current year presentation. The interim financial statements, in the opinion of management, reflect all adjustments (including normal recurring accruals) necessary for a fair statement of the results of operations for the interim periods ended June 30, 2002 and 2001.

The results of operations for the interim periods are not necessarily indicative of the results of operations to be expected for the fiscal year, although the Company expects to incur a substantial loss for the year ended December 31, 2002. These interim financial statements should be read in conjunction with the audited financial statements for the year ended December 31, 2001, which are contained in the Company's 2001 Annual Report to its stockholders and in its Form 10-K filed with the Securities and Exchange Commission.

2. ACCOUNTING POLICIES

BASIC AND DILUTED LOSS PER COMMON SHARE

Basic loss per share is based upon the weighted average number of common shares outstanding during the period. Diluted loss per share is based upon the weighted average number of common shares outstanding during the period plus additional weighted average common equivalent shares outstanding during the period when the effect is not anti-dilutive. Common equivalent shares result from the assumed exercise of outstanding stock options, the proceeds of which are then assumed to have been used to repurchase outstanding stock using the treasury stock method, and the assumed conversion of convertible notes. Common equivalent shares have not been included in the net loss per share calculations as their effect would be anti-dilutive.

The following table sets forth the computation of basic and diluted loss per common share (in thousands, except per share amounts):

	FOR THE THREE MONTHS ENDED JUNE 30,		FOR THE SIX MONTHS ENDED JUNE 30,	
	2002	2001	2002	2001
Basic and diluted net loss per common share:				
Net loss before cumulative effect of changes in accounting principles	$(21,019)	$(13,378)	$(43,086)	$(25,59
Basic and diluted weighted average number of common shares outstanding	75,660	74,381	75,408	74,15
Basic and diluted net loss per common share before cumulative effect of changes in accounting principles	$ (0.28)	$ (0.18)	$ (0.57)	$ (0.3
Anti-dilutive common equivalent shares outstanding:				
Stock options	15,746	14,161	15,746	14,16
Convertible notes	3,414	3,739	3,414	3,73

VERTEX PHARMACEUTICALS INCORPORATED

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

2. ACCOUNTING POLICIES (CONTINUED)
SEGMENT INFORMATION

On July 18, 2001, the Company completed a merger with Aurora Biosciences Corporation ("Aurora"). Aurora specialized in assay development, screening and cell biology services and instrumentation.

On March 1, 2001, Aurora completed a merger with PanVera Corporation ("PanVera"). PanVera is a biotechnology company engaged in the development, manufacture and worldwide supply of proteins and reagents for evaluation as targets and drug screening assays for high-throughput screening.

In the first quarter of 2002, following the acquisitions, the Company aligned its business into two operating segments: (i) Pharmaceuticals and (ii) Discovery Tools and Services, in an effort to further leverage the strengths of the acquired business.

The Company's Pharmaceuticals business seeks to discover, develop and commercialize major pharmaceutical products independently and with partners. The Company's Discovery Tools and Services business specializes in assay development, screening services, instrumentation and the manufacture and sale of proteins and reagents.

As of July 1, 2002, the Company began to commercialize the Aurora instruments and services business, along with PanVera's reagents and probes business, under the name PanVera LLC. PanVera LLC's core business will include the manufacture and sale of proteins, reagents, probes and instruments as well as assay development and screening services to life sciences customers. The former Aurora San Diego site operations will mainly focus on pharmaceutical drug discovery and will operate under the name Vertex Pharmaceuticals (San Diego) LLC. These changes align with the operating segments of the business.

3. CHANGE IN ACCOUNTING PRINCIPLE--REVENUE RECOGNITION

In the third quarter of 2001, in connection with an overall review of accounting policies concurrent with the merger with Aurora, Vertex elected to

change its revenue recognition policy for collaborative and other research and development revenues from the EITF 91-6 method to the substantive milestone method. Vertex believes this method is preferable because it is more reflective of the Company's on going business operations and because it is consistent with industry practices following the prior year implementation of SAB 101, "Revenue Recognition in Financial Statements," throughout the biotechnology industry. Under the new accounting method, adopted retroactively to January 1, 2001, the Company recognizes revenue from non-refundable, up-front, license and milestone payments, not specifically tied to a separate earnings process, ratably over the period of performance. Research funding is recognized as earned ratably over the period of effort. Milestones, based on designated achievement points that are considered at risk and substantive at the inception of the contract, are recognized as earned when the corresponding payment is reasonably assured. The Company evaluates whether milestones are at risk and substantive based on the contingent nature of the milestone, specifically reviewing factors such as the technological and commercial risk that needs to be overcome and the level of investment required.

Previously, the Company had recognized revenue from collaborative research and development arrangements in a manner similar to that prescribed by EITF 91-6. Under that model, revenue was recognized for non-refundable license fees, milestones, and collaborative research and development funding using the lesser of the non-refundable cash received or the result achieved using percentage of

3. CHANGE IN ACCOUNTING PRINCIPLE--REVENUE RECOGNITION (CONTINUED)
completion accounting. Where the Company had no continuing involvement, non-refundable license fees were recorded as revenue upon receipt and milestones were recorded as revenue upon achievement of the milestone by the collaborative partner.

Pursuant to this change in accounting principle, Vertex recorded a one-time non-cash charge of $25,901,000 in the first quarter of 2001. The impact of the adoption of this new accounting policy for revenue recognition for collaborative research and development revenues was to defer revenue recognition for certain portions of revenue previously recognized in prior accounting periods under our collaborative agreements into future accounting periods. The results for the three and six months ended June 30, 2001 have been restated in accordance with the new revenue recognition policy.

4. SEGMENT INFORMATION

The Company has aligned its business into two operating segments: (i) Pharmaceuticals and (ii) Discovery Tools and Services. The Company's Pharmaceuticals business seeks to discover, develop and commercialize major pharmaceutical products independently and with partners. The Company's Discovery Tools and Services business specializes in assay development, screening services, instrumentation and the manufacture and sale of proteins and reagents. The Company evaluates segment performance based on the loss before merger-related charges and the cumulative effect of the change in accounting principle. The Company does not evaluate segment performance based on the segment's total assets and therefore the Company's assets are not reported by segment. The following table presents, by segment, the results of operations for the three and six months ended June 30, 2002 and 2001. For the three and six months ended June 30, 2001, the Company was unable to restate the results of operations into the new operating segments: Pharmaceuticals and Discovery Tools and Services. Thus, for comparative purposes, the table also presents results of

operations information for

VERTEX PHARMACEUTICALS INCORPORATED

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

4. SEGMENT INFORMATION (CONTINUED)
the three and six month periods ended June 31, 2002 and 2001 by the former segments: Vertex and Aurora.

(IN THOUSANDS)	PHARMACEUTICALS	DISCOVERY TOOLS AND SERVICES	TOTA
Three Months Ended June 30, 2002:			
Revenues	$ 21,243	$21,087	$ 42,
Reportable segment income (loss)	$(32,617)	$11,598	$(21,
Six Months Ended June 30, 2002:			
Revenues	$ 41,794	$41,231	$ 83,
Reportable segment income (loss)	$(63,647)	$20,561	$(43,

(IN THOUSANDS)	VERTEX	AURORA	TOTAL
Three Months Ended June 30, 2002:			
Revenues	$ 20,973	$21,357	$ 42,330
Reportable segment income (loss)	$(23,345)	$ 2,326	$(21,019
Three Months Ended June 30, 2001:			
Revenues	$ 18,280	$22,361	$ 40,641
Reportable segment income (loss)	$(12,612)	$ 3,597	$ (9,015
Six Months Ended June 30, 2002:			
Revenues	$ 41,166	$41,859	$ 83,025
Reportable segment income (loss)	$(45,893)	$ 2,807	$(43,086
Six Months Ended June 30, 2001:			
Revenues	$ 35,715	$39,882	$ 75,597
Reportable segment income (loss)	$(23,104)	$ 3,054	$(20,050

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDE JUNE 30,	
	2002	2001	2002	200

Total loss for reportable segments	$(21,019)	$ (9,015)	$(43,086)	$(20,
Merger related charges	--	$ (4,363)	--	(5,
Cumulative effect of change in accounting principle--revenue recognition	--	--	--	(25,
Total net loss	$(21,019)	$(13,378)	$(43,086)	$(51,

VERTEX PHARMACEUTICALS INCORPORATED

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

5. COMPREHENSIVE LOSS

For the three and six months ended June 30, 2002 and 2001, respectively, comprehensive loss was as follows (in thousands):

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2002	2001	2002	2001
Net loss	$(21,019)	$(13,378)	$(43,086)	$(51,493)
Changes in other comprehensive loss:				
Unrealized holding gains (losses) on marketable securities	1,299	(37)	(4,742)	5,244
Foreign currency translation adjustment	413	(39)	262	(436)
Total change in other comprehensive loss	1,712	(76)	(4,480)	4,808
Total comprehensive loss	$(19,307)	(13,454)	$(47,566)	$(46,685)

6. LEGAL PROCEEDINGS

Chiron Corporation (Chiron) filed suit on July 30, 1998 against Vertex and Eli Lilly and Company in the United States District Court for the Northern District of California, alleging infringement by the defendants of three U.S. patents issued to Chiron. The infringement action relates to research activities by the defendants in the hepatitis C viral protease field and the alleged use of inventions claimed by Chiron in connection with that research. Chiron has requested damages in an unspecified amount, as well as an order permanently enjoining the defendants from unlicensed use of the claimed Chiron inventions. During 1999, Chiron requested and was granted a reexamination by the U.S. Patent and Trademark Office of all three of the patents involved in the suit. Chiron also requested and, over the opposition of Vertex and Eli Lilly, was granted a stay in the infringement lawsuit, pending the outcome of the patent reexamination. That reexamination proceeding is still on-going and the stay is still in effect. However, a Reexamination Certificate has been issued in two of the three Chiron patents in suit. While the length of the stay and the final outcome of the lawsuit cannot be determined, Vertex maintains that Chiron's claims are without merit and intends to defend the lawsuit, if and when it resumes, vigorously.

On December 7, 2001 Oregon Health Sciences University filed suit against Vertex in the District Court of Oregon. The complaint in the suit seeks to name Dr. Bruce Gold, an employee of Oregon Health Sciences University, as an inventor and Oregon Health Sciences University as part owner of five of Vertex's neurophilin patents and associated damages. The suit stems from assays run on Vertex compounds by Dr. Gold under a sponsored research agreement in 1996. Vertex has investigated the inventorship on these patents and believes that Dr. Gold is not an inventor, Oregon Health Sciences has no ownership interest in any of these patents, and that the claims made in this complaint are without merit. Vertex intends to contest this claim vigorously. We believe, based on information currently available, that the ultimate outcome of the action will not have a material impact on the Company's consolidated financial position.

7. RECENT ACCOUNTING PRONOUNCEMENTS

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets," which requires that ratable amortization of goodwill be replaced with periodic tests of the goodwill's impairment and that intangible assets other than goodwill be amortized over their useful lives. The provisions of SFAS No. 142 are effective for fiscal years beginning after December 15, 2001. The Company adopted the provisions of SFAS 142 on January 1, 2002 as required; the adoption did not have a material effect on the Company's financial position and results of operations.

In October 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment of Long-Lived Assets." SFAS No. 144 supercedes SFAS No. 121 "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of" and provides a single accounting model for long-lived assets to be disposed of. The provisions of SFAS No. 144 are effective for fiscal years beginning after December 15, 2001. The Company adopted the provisions of SFAS 144 on January 1, 2002 as required; the adoption did not have a material effect on the Company's financial position and results of operations.

In April 2002, the FASB issued SFAS No. 145, "Rescission of FASB Nos. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections as of April 2002." This Statement rescinds FASB No. 4, "Reporting Gains and Losses from Extinguishment of Debt," and an amendment of that Statement and FASB Statement No. 64, "Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements" and SFAS No. 44, "Accounting for Intangible Assets of Motor Carriers." SFAS No. 145 also amends SFAS No. 13, "Accounting for Leases," to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have the same economic effect as a sale-leaseback transaction. SFAS No. 145 also amends other existing authoritative pronouncements to make various technical corrections, clarify meanings, or describe their applicability under changed conditions. Adoption of certain provisions of this standard was required after May 15, 2002, while other provisions must be adopted within financial statements issued after May 15, 2002 or the year beginning after May 15, 2002. The Company is currently evaluating the potential impact of SFAS No. 145 on its financial position and results of operations.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," which supersedes EITF 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." The standard affects the accounting for restructuring charges and related activities. The provisions of this statement are required to be adopted for exit or disposal activities that are initiated after December 31, 2002.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

We are a global biotechnology company with more than 1,000 employees located in Cambridge, MA, Madison, WI, San Diego, CA and Abingdon, UK. We have two operating segments: Pharmaceuticals and Discovery Tools and Services.

Our Pharmaceuticals business seeks to discover, develop, and commercialize major pharmaceutical products independently and with collaborators. Chemogenomics, our proprietary, systematic, genomics-based platform, is designed to accelerate the discovery of new drugs and to expand intellectual property coverage of drug candidate compounds and classes of related compounds. We believe this approach, which targets gene families, has formed the basis for successful drug discovery and for the advancement of drug candidates by Vertex and its collaborators.

Our first approved product is Agenerase-Registered Trademark- (amprenavir), an HIV protease inhibitor, which we co-promote with GlaxoSmithKline. We earn a royalty from GlaxoSmithKline on sales of Agenerase. Agenerase has received approval in 34 countries worldwide, including the United States, the 15 member states of the European Union (E.U.), and Japan, where the drug is sold under the trade name Prozei-TM-. We have more than twelve drug candidates in development to treat viral diseases, cancer, autoimmune and inflammatory diseases, neurological disorders and genetic disorders. We have significant collaborations with large pharmaceutical companies including Aventis, Eli Lilly, GlaxoSmithKline, Novartis, and Serono. We are developing several drug candidates in commercial collaborations in which we retain rights to downstream product revenue.

Our Discovery Tools and Services business specializes in assay development, screening services, instruments and products, and the manufacture and sale of proteins and reagents. This business has collaborations with large pharmaceutical companies for assay development, screening services and the development of specialized screening platforms, as well as the sale of proteins and reagents to the pharmaceuticals industry.

Our Discovery Tools and Services business has contracts in place that require the delivery of products, licenses and services throughout 2002. These contracts account for more than $65 million of actual plus potential 2002 revenue of which approximately $12 million relates to one specific contract.

Our collaborations and contracts in the Pharmaceuticals and Discovery Tools and Services businesses provide us with financial support and other valuable resources for our research programs, development of our clinical drug candidates, and marketing and sales of our products. We believe that we are positioned to commercialize multiple products in the coming years, which we expect will generate increased milestone payments, product revenues and royalty payments.

We have incurred operating losses since our inception and expect to incur losses for the foreseeable future. We plan to make significant investments in research and development for our other potential products. We expect that losses will fluctuate from year to year and that such fluctuations may be substantial.

In the third quarter of 2001, in connection with our overall review of accounting policies concurrent with our merger with Aurora, we elected to change our revenue recognition policy for collaborative and other research and development revenues from the Emerging Issues Task Force No. 91-6 (EITF 91-6) method to the Substantive Milestone Method. We believe this method is preferable because it is reflective of the Company's on-going business operations and is

more consistent with industry practices following the prior year implementation of SAB 101 throughout the biotechnology industry.

The cumulative effect of the 2001 change in accounting principle related to revenue recognition recorded in the third quarter of 2001, retroactive to January 1, 2001, resulted in a non-cash charge to income of $25,901,000 in the first quarter of 2001. Included in the charge to income was $1,591,000 and

$3,182,000 of revenue recognized in the three and six months ended June 30, 2002 and $1,889,000 and $3,714,000 of revenue recognized in the three and six months ended June 30, 2001, respectively.

CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of our financial condition and results of operations is based upon our condensed consolidated financial statements that are unaudited and have been prepared in accordance with generally accepted accounting principles in the United States of America. The preparation of these financial statements requires us to make certain estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenue and expense during the reported periods. These items are constantly monitored and analyzed by management for changes in facts and circumstances, and material changes in these estimates could occur in the future. Changes in estimates are recorded in the period in which they become known. We base our estimates on historical experience and various other assumptions that we believe to be reasonable under the circumstances. Actual results may differ from our estimates if past experience or other assumptions do not turn out to be substantially accurate.

In December 2001, the SEC requested that all registrants discuss their "critical accounting policies" in management's discussion and analysis of financial condition and results of operations. The SEC indicated that a "critical accounting policy" is one that is both important to the portrayal of the company's financial conditions and results, and requires management's most difficult, subjective or complex judgments, often as a result of the need to makes estimates about the effect of matters that are inherently uncertain. While our significant accounting polices are more fully described in Note B to our consolidated financial statements included in our Form 10-K, we believe our revenue recognition policy to be critical and have outlined this policy below.

Our revenue recognition policies are in accordance with the SEC's Staff Accounting Bulletin No. 101 (SAB 101), "Revenue Recognition in Financial Statements". We generate revenue through collaborative research and development agreements, product sales, assay development and screening services and royalty agreements.

Our collaborative research and development revenue is primarily generated through collaborative research and development agreements with strategic partners for the development of small molecule drugs that address major unmet medical needs. The terms of the agreements typically include non-refundable up-front license fees, funding of research and development efforts, payments based upon achievement of certain at-risk and substantive milestones and royalties on product sales.

Under the Substantive Milestone Method, adopted retroactively to January 1, 2001, we recognize revenue from non-refundable, up-front license fees and milestones, not specifically tied to a separate earnings process, ratably over the contracted or estimated period of performance. Changes in estimates could impact revenue in the period the estimate is changed. Research funding is

recognized as earned, ratably over the period of effort. Milestones that are based on designated achievement points and that are considered at risk and substantive at the inception of the collaborative contract, are recognized as earned, when the corresponding payment is considered reasonably assured. We evaluate whether milestones are at risk and substantive based on the contingent nature of the milestone, specifically reviewing factors such as the technological and commercial risk that must be overcome and the level of investment required.

Product sales include instrumentation system sales, technology licensing and biotechnology product sales as well as commercial drug substance sales. Revenue from licenses where we have continuing obligations is recognized over the period of the license. Revenue from perpetual licenses is recognized when the license is issued, provided that there are no significant continuing obligations and the payment is non-refundable and non-creditable.

Revenue from sales of commercial drug substance, biotechnology products and certain instrumentation system sales, is recognized upon shipment, when the title to the product and associated risk of loss has passed to the customer, collectibility is reasonably assured and upon acceptance when acceptance criteria are specified or upon expiration of the acceptance period, if applicable. Sales under long-term production contracts are recognized using percentage of completion accounting, based on actual costs incurred to date compared to total estimated costs to complete. Funding for prototype instrumentation systems was recognized ratably over the terms of the agreements, which approximated costs incurred. Milestones related to delivery of the components of the prototype systems were recognized when earned, as evidenced by written acknowledgement of acceptance from the customer.

Service revenues include assay development, screening services and contracted product development. Service revenue is recognized as the services are performed or ratably over the service period if we believe such method will approximate the expense being incurred. Revenue from upfront fees is deferred and recognized over the service period.

Our subsidiary has certain contracts under which it agrees to sell instrumentation systems and technology licenses in addition to providing assay development and screening services. Each of these separable elements may be individually delivered and is not considered essential to the functionality of the others. We allocate revenue under such contracts to each of the separable elements based on the relative fair value of each element, which under most of our agreements approximates the stated price in the contract.

Royalty revenue is recognized based upon actual and estimated net sales of licensed products in licensed territories, as provided by our collaborative partner, and is generally recognized in the period the sales occur. Differences between actual royalty revenues and estimated royalty revenues, which have not been historically significant, are reconciled and any resulting adjustments are made in the quarter they become known.

THREE MONTHS ENDED JUNE 30, 2002 COMPARED WITH THREE MONTHS ENDED JUNE 30, 2001

Our net loss for the three months ended June 30, 2002 was $21,019,000 or $0.28 per basic and diluted common share compared to a loss before merger related costs of $9,015,000, or $0.12 per basic and diluted common share, for the three months ended June 30, 2001. The net loss for the three months ended June 30, 2001, including merger related costs of $4,363,000, was $13,378,000 or $0.18 per basic and diluted common share.

Total revenues increased to $42,330,000 for the three months ended June 30,

2002 compared to $40,641,000 for the three months ended June 30, 2001. In the second quarter of 2002, Pharmaceuticals revenue was comprised of $2,384,000 in royalties and $18,859,000 in collaborative research and development revenue, as compared with $2,862,000 in royalties and $16,273,000 in collaborative research and development revenue in the second quarter of 2001. In the second quarter of 2002, Discovery Tools and Services revenue was comprised of $15,587,000 in product sales and royalties and $5,500,000 in service revenue, as compared with $15,423,000 in product sales and royalties and $6,083,000 in service revenue in the second quarter of 2001.

Pharmaceuticals royalties consist primarily of Agenerase royalty revenue. Agenerase royalty revenue is based on actual and estimated worldwide net sales of Agenerase.

Collaborative research and development revenue consists of research support payments, development reimbursements, milestones and amortization of previously received up-front or license payments.

Collaborative research and development revenue increased in the second quarter of 2002 by 16%, or $2,586,000, as compared with the second quarter of 2001 due primarily to additional revenue earned under the Novartis collaboration. In the second quarter of 2002, we recognized $10,434,000 of revenue

under the Novartis collaboration compared with $8,512,000 in the second quarter of 2001. Effort related to our kinase research program increased significantly in the first and second quarters of 2002 compared to 2001. Also, during the second quarter of 2002 development reimbursements from certain collaborators increased.

Product sales and royalties include instrumentation sales, technology licensing and biotechnology product sales.

Product sales increased $164,000, or 1%, to $15,587,000 in the second quarter of 2002 from $15,423,000 in the second quarter of 2001. The increase in product sales is due primarily to increased technology licensing during the quarter offset by decreased instrumentation revenue and biotechnology product revenue.

Service revenue includes assay development, screening services and contracted product development.

Service revenue decreased $583,000, or 10%, to $5,500,000 in the second quarter of 2002 from $6,083,000 in the second quarter of 2001. The decrease is a result of the completion of several significant screening agreements in late 2001.

Pharmaceutical royalty costs of $828,000 and $972,000 in the second quarter of 2002 and 2001, respectively, consist primarily of royalty payments on the sales of Agenerase.

Product costs decreased $4,166,000, or 61%, to $2,662,000 in the second quarter of 2002 from $6,828,000 in the second quarter of 2001. The decrease in product costs is attributable to a strategic shift in focus of the Discovery Tools and Services business towards technology licensing and discovery tools which have higher gross margins, and away from product sales. Product gross margins will fluctuate from period to period based upon the product mix.

Cost of service revenue in our Discovery Tools and Services business increased $576,000, or 24%, to $2,972,000 in the second quarter of 2002 from

$2,396,000 in the second quarter of 2001. The increase is primarily due to increased overhead related to these service agreements.

Research and development expenses increased $11,969,000, or 35%, to $46,546,000 in the second quarter of 2002 from $34,577,000 in the second quarter 2001 primarily due to our continued investment in advancing our broad clinical pipeline and fueling our drug discovery engine. Our clinical investment was primarily focused on the advancement of our second generation p38 MAP kinase, caspase and IMPDH inhibitors. We currently are focusing these oral drugs on large market opportunities such as inflammatory, autoimmune and viral diseases. We continued to expand our multi-target gene family research programs, of which kinases is our most advanced, along with investments in target families such as proteases and ion channels. As a result of our continued expansion, personnel and facilities expenses also increased.

Sales, general and administrative expenses increased $1,968,000, or 17%, to $13,348,000 for the three months ended June 30, 2002 from $11,380,000 for the three months ended June 30, 2001. This increase is primarily attributable to increased personnel and professional expenses as well as the write-off of certain land development costs. We believe we have a solid infrastructure necessary to support our growth and will continue to manage our investments prudently. In addition, legal and patent expenses have increased in the period as we continue to protect our intellectual property and contest a suit filed by Oregon Health Sciences University. We believe, based on information currently available, that the ultimate outcome of the action will not have a material impact on our consolidated financial position.

Interest income decreased approximately $4,301,000 to approximately $7,467,000 in the second quarter of 2002 from $11,768,000 in the second quarter of 2001. This reflects a lower interest rate environment as well as a lower level of invested funds compared to the prior year.

Interest expense decreased $811,000 to approximately $4,460,000 in the second quarter of 2002 from $5,271,000 in the second quarter of 2001. The decrease in interest expense is a result of the reduction in principal amount of our convertible notes from $345,000,000 at June 30, 2001 to $315,000,000 at June 30, 2002. In October 2001, we repurchased $30,000,000 in principal amount of our 5% convertible subordinated notes due September 2007.

SIX MONTHS ENDED JUNE 30, 2002 COMPARED WITH SIX MONTHS ENDED JUNE 30, 2001

The net loss for the six months ended June 30, 2002 was $43,086,000 or $0.57 per basic and diluted share, compared to a loss before our change in accounting principle and merger related costs of $20,050,000, or $0.27 per basic and diluted common share, for the six months ended June 30, 2001. The net loss for the six months ended June 30, 2001, including merger related costs of $5,542,000 and the cumulative effect of the change in accounting principle of $25,901,000, was $51,493,000 or $0.69 per basic and diluted common share.

Total revenues increased to $83,025,000 for the six months ended June 30, 2002 from $75,597,000 for the six months ended June 30, 2001.

Collaborative research and development revenue increased $5,090,000, or 16%, to $36,936,000 for the six months ended June 30, 2002 as compared with $31,846,000 for the six months ended June 30, 2001 primarily due to additional revenue earned under the Novartis collaboration. For the six months ended June 30, 2002, we recognized $20,466,000 of revenue under the Novartis collaboration compared with $15,623,000 for the six months ended June 30, 2001. Effort related to our kinase research program increased significantly in the first and second quarters of 2002 compared to 2001.

Product sales and royalties increased $3,845,000, or 14%, to $30,797,000 for the six months ended June 30, 2002 from $26,952,000 for the six months ended June 30, 2001. The increase in product sales is due primarily to increased technology licensing revenue offset by decreased instrumentation revenue and biotechnology product revenue.

Services revenue decreased $907,000, or 8%, to $10,434,000 for the six months ended June 30, 2002 from $11,341,000 for the six months ended June 30, 2001. The decrease is a result of the completion of several screening agreements in late 2001.

Product costs decreased $6,444,000, or 47%, to $7,252,000 for the six months ended June 30, 2002 from $13,696,000 for the six months ended June 30, 2001. The decrease in product costs is attributable to a strategic shift in focus of the Discovery Tools and Services business toward technology licensing and discovery tools which have higher gross margins, and away from product sales.

Cost of service revenue in our Discovery Tools and Services business increased $1,020,000, or 20%, to $6,206,000 for the six months ended June 30, 2002 from $5,186,000 for the six months ended June 30, 2001. Cost of services increased as a result of increased personnel and professional expenses.

Research and development costs increased $26,451,000, or 39%, to $93,568,000 for the six months ended June 30, 2002 from $67,117,000 for the six months ended June 30, 2001 primarily due to our continued investment in advancing our broad clinical pipeline and fueling our drug discovery engine.

We have more than 12 drug candidates in development targeting a range of major diseases. Our collaborative partners have agreed to fund portions of our research and development programs and/or to conduct certain research and development related to specified drug candidates. The following table

details our Collaborator and Company-sponsored research and development expenses for the three and six months ended June 30 (in thousands):

	FOR THE THREE MONTHS ENDED JUNE 30, 2002			FOR THE SIX MON ENDED JUNE 3	
	RESEARCH	DEVELOPMENT	TOTAL	RESEARCH	DEVELOPM
Collaborator-Sponsored.....	$14,558	$ 8,318	$22,876	$29,221	$15,74
Company-Sponsored.....	15,994	7,676	23,670	31,235	17,37
Total.....	$30,552	$15,994	$46,546	$60,456	$33,11

	FOR THE THREE MONTHS ENDED JUNE 30, 2001			FOR THE SIX MON ENDED JUNE 3	
	RESEARCH	DEVELOPMENT	TOTAL	RESEARCH	DEVELOPM
Collaborator-Sponsored.....	$13,750	$ 2,902	$16,652	$24,702	$ 8,09

Company-Sponsored.....	9,642	8,283	17,925	21,029	13,29
Total.....	$23,392	$11,185	$34,577	$45,731	$21,38

To date we have incurred in excess of $724,000,000 in research and development costs associated with drug discovery and development. These costs include discovery costs associated with our kinase, protease and ion channel gene family programs and our other discovery programs, as well as development costs incurred in advancing drug candidates that were products of these discovery programs. Our major development investments relate to the drug candidates identified on the table appearing on the following page. We anticipate research and development expenses will continue to increase as we add personnel and expand research and development activities to accommodate our existing collaborations and additional commitments we may make.

We estimate that it takes from 10 to 15 years (industry average is 12 years) to discover, develop and bring to market a pharmaceutical product. Drug development in the United States is a process that includes several steps defined by the FDA as outlined below:

PHASE:	OBJECTIVE:	ESTIMATED DUR
Discovery	Lead identification and target validation	2 to 4 years
DEVELOPMENT		
Pre-Clinical	Toxicology to identify risks for humans; gather early pharmacokentic data	1 to 2 years
Phase I	Establish safety in humans, study how the drug works, metabolizes and interacts with other drugs	1 to 2 years
Phase II	Explore effectiveness of the drug and its optimal dosage	2 to 4 years
Phase III	Confirm efficacy, dose regimen and safety profile of the drug	2 to 4 years
FDA approval	Approval by the FDA to sell and market the drug under certain prescribed labeling	6 months to 2

The successful development of our products is highly uncertain and subject to a number of risk factors. The duration of clinical trials may vary substantially according to the type, complexity and novelty of the pharmaceutical product. The FDA and comparable agencies in foreign countries impose substantial requirements on the introduction of therapeutic pharmaceutical products through lengthy and detailed laboratory and clinical testing procedures, sampling activities and other costly and time-consuming procedures. Data obtained from pre-clinical and clinical activities are susceptible to varying interpretations, which could delay, limit or prevent regulatory approval. The duration and the cost related to discovery, pre-clinical and clinical trials may vary significantly over the life of a project and are difficult to predict. The most significant costs associated with drug discovery and development are those costs associated with Phase II and Phase III clinical trials. Due to the variables described above, we are not able to estimate precisely the costs to complete these research and development programs.

Below is a summary of our drug candidates currently in pre-clinical and

clinical development:

DRUG	CLINICAL INDICATIONS	PHASE	PROGRAM	COLLAB
INFECTIOUS DISEASE				
VX-175 (GW433908 or 908)	HIV	III	Protease (HIV)	GlaxoS
Merimepodib (VX-497)	Chronic hepatitis C	II	IMPDH	--
VX-950	Chronic hepatitis C	Preclin	Protease (HCV)	Eli Li
VX-799	Sepsis	Preclin	Caspases	Serono
VX-385	HIV	Preclin	Protease (HIV)	GlaxoS
INFLAMMATION AND AUTOIMMUNE DISEASE				
Pralnacasan (VX-740)	Rheumatoid arthritis (RA); osteoarthritis (OA)	II	ICE	Aventi
VX-148	Psoriasis; autoimmune diseases	I	IMPDH	--
VX-702	Inflammatory diseases	I	p38 MAP Kinase	Kissei East)
VX-944	Various	Preclin	IMPDH	--
VX-765	Inflammatory diseases	Preclin	ICE	--
VX-850	Inflammatory diseases	Preclin	p38 MAP Kinase	Kissei East)
CANCER				
Incel-TM-	Multidrug resistant solid tumor cancers	II	MDR	--
VX-853	Multidrug resistant solid tumor cancers	I/II	MDR	--
GENETIC DISORDERS				
VX-563	Multiple indications	Preclin	Histone Deacetylase	--

Currently, our discovery operations are focused significantly on the kinase research program with Novartis. Other significant discovery programs include ion channels, proteases, caspases and gyrase. Our development investment is primarily focused on the advancement of our second-generation p38 MAP kinase program (VX-702 and VX-850), IMPDH program (VX-148, VX-497 and VX-944) and ICE program (VX-765). Our collaborative partners are advancing other significant late stage drug candidates such as VX-175, targeted at HIV, and Pralnacasan (VX-740), currently targeting rheumatoid arthritis and osteoarthritis. Our partners bear the costs of the continued development of these drugs.

We organize our research and development efforts based on the drug target or target gene family. The programs detailed above identify the targets for therapeutic intervention.

Sales, general and administrative expenses increased $2,114,000, or 9%, to $24,443,000 for the six months ended June 30, 2002 from $22,329,000 for the six months ended June 30, 2001. The increase is primarily related to increased personnel and professional expenses as well as increased legal expenses as we continue to protect our intellectual property and contest a suit filed by Oregon Health Sciences University.

Interest income decreased $8,913,000 to approximately $15,925,000 for the six months ended June 30, 2002 from $24,838,000 for the six months ended June 30, 2001. The decrease is a result of lower funds invested and lower portfolio yields.

Interest expense decreased $1,382,000 to approximately $8,922,000 for the six months ended June 30, 2002 from $10,304,000 for the six months ended June 30, 2001. The decrease is a result of the reduction in principal amount of our convertible notes from $345,000,000 at June 30, 2001 to $315,000,000 at June 30, 2002. In October 2001, we repurchased $30,000,000 in principal amount of our 5% convertible subordinated notes due September 2007.

LIQUIDITY AND CAPITAL RESOURCES

Our operations have been funded principally through strategic collaborative agreements, strategic technology alliances, revenues from assay development and screening services, product sales, royalties, public offerings and private placements of our equity and debt securities, equipment lease financing, and investment income. With the approval and launch of Agenerase in April 1999, we began receiving product royalty revenues. In 2000, we completed private placements of $175,000,000 of 5% Convertible Subordinated Notes due March 2007 and $345,000,000 of 5% Convertible Subordinated Notes due September 2007.

We have continued to increase and advance products in our research and development pipeline. Consequently, we expect to incur losses on a quarterly and annual basis as we continue to develop existing and future compounds and to conduct clinical trials of potential drugs. We also expect to incur substantial administrative and commercialization expenditures in the future and additional expenses related to filing, prosecution, defense and enforcement of patent and other intellectual property rights.

We expect to finance these substantial cash needs with future payments under our existing and future collaborative agreements, strategic technology alliances, royalties from the sales of Agenerase, revenues from assay development and screening services, product sales, existing cash and marketable securities of $679,845,000 at June 30, 2002, together with investment income earned thereon, and facilities and equipment financing. To the extent that funds from these sources are not sufficient to fund our activities, it will be necessary to raise additional funds through public offerings or private placements of securities or other methods of financing. There can be no assurance that such financing will be available on acceptable terms, if at all.

Our aggregate cash and marketable securities decreased $63,357,000 to $679,845,000, which includes cash and cash equivalents of $125,268,000, at June 30, 2002 from $743,202,000, including cash and cash equivalents of $189,205,000, at December 31, 2001. Net cash used in operations was $47,777,000 for the six months ended June 30, 2002. Included in the cash used in operations was the net loss of $43,086,000 and a decrease in deferred revenue of $13,146,000, partially offset by $11,986,000 of non-cash charges and gains. Deferred revenue decreased due to cash received for research funding and the receipt of a milestone payment in late 2001. Such cash was based on contractual commitments that are being fulfilled in 2002 and 2003. Cash used by investing activities for the six months ended June 30, 2002 was $22,783,000, including net purchases of available-for-sale securities of $4,306,000 and property and equipment expenditures of $18,258,000 as we continue to invest in our infrastructure and drug discovery technology. Cash provided by financing activities during the six months ended June 30, 2002 was $6,361,000 including $8,717,000 from the issuance of common stock under employee stock option and benefit plans offset by $2,356,000 in principal payments on capital leases and other obligations. The decrease in cash and marketable securities can fluctuate from quarter to quarter.

FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements about our business,

including our expectation that (i) we are positioned to commercialize multiple products in the coming years that we expect will generate increased revenues, (ii) our losses will continue, (iii) our research and development expenses, our administrative and commercialization expenses and our expenses related to filing, prosecuting and defending our patents and intellectual property rights will increase, and sales, general and administrative expenses will remain consistent with current levels, and (iv) the Chiron Corporation and Oregon Health Sciences University litigation will not have a material adverse effect on us. While management makes its best efforts to be accurate in making forward-looking statements, such statements are subject to risks and uncertainties that could cause our actual results to vary materially. These risks and uncertainties include, among other things, our inability to successfully integrate Aurora

into our existing business, our inability to further identify, develop and achieve commercial success for new products and technologies, the possibility of delays in the research and development necessary to select drug development candidates and delays in clinical trials, the risk that clinical trials may not result in marketable products, the risk that we may be unable to successfully finance and secure regulatory approval of and market our drug candidates, our dependence upon pharmaceutical and biotechnology collaborations, the levels and timing of payments under our collaborative agreements, uncertainties about our ability to obtain new corporate collaborations and acquire new technologies on satisfactory terms, if at all, the development of competing systems, our ability to protect our proprietary technologies, patent-infringement claims, risks of new, changing and competitive technologies and regulations in the U.S. and internationally. Please see the "Risk Factors" appearing in our 2001 Annual Report to Stockholders and in our Form 10-K filed with the Securities and Exchange Commission for more details regarding these and other risks. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

LEGAL PROCEEDINGS

Chiron Corporation filed suit on July 30, 1998 against Vertex and Eli Lilly and Company in the United States District Court for the Northern District of California, alleging infringement by the defendants of three U.S. patents issued to Chiron. The infringement action relates to research activities by the defendants in the hepatitis C viral protease field and the alleged use of inventions claimed by Chiron in connection with that research. Chiron has requested damages in an unspecified amount, as well as an order permanently enjoining the defendants from unlicensed use of the claimed Chiron inventions. During 1999, Chiron requested and was granted a reexamination by the U.S. Patent and Trademark Office of all three of the patents involved in the suit. Chiron also requested and, over the opposition of Vertex and Eli Lilly, was granted a stay in the infringement lawsuit, pending the outcome of the patent re-examination. That reexamination proceeding is still on-going and the stay is still in effect. However, a Reexamination Certificate has been issued in two of the three Chiron patents in suit. While the length of the stay and the final outcome of the lawsuit cannot be determined, we maintain that Chiron's claims are without merit and we intend to defend the lawsuit, if and when it resumes, vigorously.

On December 7, 2001 Oregon Health Sciences University filed suit against Vertex in the District Court of Oregon. The complaint in the suit seeks to name Dr. Bruce Gold, an employee of Oregon Health Sciences University, as an inventor and Oregon Health Sciences University as part owner of five of Vertex's neurophilin patents, and associated damages. The suit stems from assays run on Vertex compounds by Dr. Gold under a sponsored research agreement in 1996. We have investigated the inventorship on these patents and believe that Dr. Gold is

not an inventor, Oregon Health Sciences has no ownership interest in any of these patents, and that the claims made in this complaint are without merit. We intend to contest this claim vigorously.

RECENT ACCOUNTING PRONOUNCEMENTS

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets," which requires that ratable amortization of goodwill be replaced with periodic tests of the goodwill's impairment and that intangible assets other than goodwill be amortized over their useful lives. The provisions of SFAS No. 142 are effective for fiscal years beginning after December 15, 2001. We adopted the provisions of SFAS 142 on January 1, 2002 as required. That adoption did not have any effect on our financial position and results of operations.

In October 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment of Long-Lived Assets." SFAS No. 144 supercedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of" and provides a single accounting model for

long-lived assets to be disposed of. The provisions of SFAS No. 144 are effective for fiscal years beginning after December 15, 2001. We adopted the provisions of SFAS 144 on January 1, 2002 as required. That adoption did not have any effect on our financial position and results of operations.

In April 2002, the FASB issued SFAS No. 145, "Rescission of FASB Nos. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections as of April 2002." This Statement rescinds FASB No. 4, "Reporting Gains and Losses from Extinguishment of Debt," and an amendment of that Statement and FASB Statement No. 64, "Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements" and SFAS No. 44, "Accounting for Intangible Assets of Motor Carriers." SFAS No. 145 also amends SFAS No. 13, "Accounting for Leases," to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have the same economic effect as a sale-leaseback transaction. SFAS No. 145 also amends other existing authoritative pronouncements to make various technical corrections, clarify meanings, or describe their applicability under changed conditions. Adoption of certain provisions of this standard was required after May 15, 2002, while other provisions must be adopted within financial statements issued after May 15, 2002 or the year beginning after May 15, 2002. We are currently evaluating the potential impact of SFAS No. 145 on our financial position and results of operations.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," which supersedes EITF 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." The standard affects the accounting for restructuring charges and related activities. The provisions of this statement are required to be adopted for exit or disposal activities that are initiated after December 31, 2002.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As part of its investment portfolio, Vertex owns financial instruments that are sensitive to market risks. The investment portfolio is used to preserve Vertex's capital until it is required to fund operations, including Vertex's research and development activities. None of these market risk sensitive instruments are held for trading purposes. Vertex does not have derivative financial instruments in its investment portfolio.

INTEREST RATE RISK

Vertex invests its cash in a variety of financial instruments, principally securities issued by the U.S. government and its agencies, investment grade corporate bonds and notes and money market instruments. These investments are denominated in U.S. dollars. All of its interest-bearing securities are subject to interest rate risk, and could decline in value if interest rates fluctuate. Substantially all of Vertex's investment portfolio consists of marketable securities with active secondary or resale markets to help ensure portfolio liquidity, and Vertex has implemented guidelines limiting the term to maturity of its investment instruments. Due to the conservative nature of these instruments, Vertex does not believe that it has a material exposure to interest rate risk.

PART II. OTHER INFORMATION

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Company's Annual Meeting of Stockholders was held on May 17, 2002.

The stockholders elected Roger W. Brimblecombe, Donald R. Conklin and Stuart J.M. Collinson to the class of directors whose term expires in 2005. The tabulation of votes with respect to the election of such directors is as follows:

	TOTAL VOTE FOR:	TOTAL VOTE WITHHELD:
Roger W. Brimblecombe.....	59,899,183	236,335
Donald R. Conklin.....	59,614,285	521,233
Stuart J.M. Collinson.....	59,857,607	277,911

In addition, the stockholders approved amendments to the Vertex Pharmaceuticals Incorporated Employee Stock Purchase Plan, including an amendment to increase the total number of shares of common stock authorized for issuance under that plan by 600,000, by a vote of 54,195,646 shares in favor, 5,687,763 shares against, and 252,109 shares abstaining.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

None

(b) Reports on Form 8-K:

On May 24, 2002, we filed a Report on Form 8-K dated May 23, 2002, Item 5, reporting that Lynne H. Brum, the Company's Vice President of Corporate Development and Communications, entered into a plan with Goldman, Sachs & Co., pursuant to which Goldman will undertake to sell, subject to a limit order, an aggregate of 23,816 shares of the Company's stock issuable upon exercise of options held by Ms. Brum.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the

registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

VERTEX PHARMACEUTICALS INCORPORATED

August 14, 2002

By: /s/ IAN F. SMITH

Ian F. Smith
VICE PRESIDENT AND
CHIEF FINANCIAL OFFICER