IDEC PHARMACEUTICALS CORP / DE
Form 10-Q
November 15, 2002

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# UNITED STATES
# SECURITIES AND EXCHANGE COMMISSION
# Washington, D.C. 20549

# FORM 10-Q

**(Mark One)**

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

**For the quarterly period ended September 30, 2002**

**OR**

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

**For the transition period from to**
**Commission file number: 0-19311**

# IDEC PHARMACEUTICALS CORPORATION

(Exact name of registrant as specified in its charter)

| **Delaware** | **33-0112644** |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

**3030 Callan Road, San Diego, CA 92121**
(Address of principal executive offices) (Zip code)

**(858) 431-8500**
(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 ý No o

As of October 31, 2002 the Registrant had 153,032,752 shares of its common stock, $.0005 par value, issued and outstanding.

**IDEC PHARMACEUTICALS CORPORATION**

**FORM 10-Q QUARTERLY REPORT**
**FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2002**

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## PART I FINANCIAL INFORMATION

### Item 1. Financial Statements.

**IDEC PHARMACEUTICALS CORPORATION AND SUBSIDIARIES**

**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

**(In thousands, except per share data)**

**(unaudited)**

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2002 | 2001 | 2002 | 2001 |
| Revenues: | | | | |
| Product sales | $ 4,958 | $ | $ 8,258 | $ |
| Revenues from unconsolidated joint business | 98,613 | 68,525 | 269,250 | 175,155 |
| Corporate partner revenues | 127 | 1,090 | 3,062 | 15,847 |
| Total revenues | 103,698 | 69,615 | 280,570 | 191,002 |
| Operating costs and expenses: | | | | |
| Cost of sales | 232 | | 1,121 | |
| Research and development | 25,367 | 20,751 | 67,596 | 63,912 |

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| Selling, general and administrative | 23,798 | 12,991 | 65,865 | 36,125 |
| Total operating costs and expenses | 49,397 | 33,742 | 134,582 | 100,037 |
| Income from operations | 54,301 | 35,783 | 145,988 | 90,965 |
| Interest income, net | 4,838 | 6,977 | 13,237 | 24,957 |
| Income before income tax provision | 59,139 | 42,850 | 159,225 | 115,922 |
| Income tax provision | 20,699 | 15,893 | 55,729 | 43,005 |
| Net income | $ 38,440 | $ 26,957 | $ 103,496 | $ 72,917 |
| Earnings per share: | | | | |
| Basic | $ 0.25 | $ 0.18 | $ 0.68 | $ 0.49 |
| Diluted | $ 0.22 | $ 0.16 | $ 0.60 | $ 0.42 |
| Shares used in calculation of earnings per share: | | | | |
| Basic | 152,679 | 152,061 | 152,977 | 150,142 |
| Diluted | 178,362 | 167,394 | 180,096 | 181,278 |

See accompanying notes to the condensed consolidated financial statements.



**IDEC PHARMACEUTICALS CORPORATION AND SUBSIDIARIES**

**CONDENSED CONSOLIDATED BALANCE SHEETS**

**(In thousands, except par value)**

| | September 30, 2002 | December 31, 2001 |
|---|---|---|
| | (unaudited) | |
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 402,765 | $ 425,999 |
| Securities available-for-sale | 544,609 | 197,824 |
| Accounts receivable | 16,555 | 6,198 |
| Due from related parties, net | 84,688 | 67,651 |
| Inventories | 23,708 | 524 |
| Prepaid expenses and other current assets | 4,655 | 1,847 |
| Total current assets | 1,076,980 | 700,043 |
| Long-term securities available-for-sale | 507,289 | 242,784 |
| Property and equipment, net | 202,817 | 108,588 |
| Deferred tax assets, net | 60,522 | 67,044 |
| Restricted cash | 22,500 | 5,002 |
| Other assets | 39,324 | 9,267 |

| | September 30, 2002 | December 31, 2001 |
|---|---|---|
| | $ 1,909,432 | $ 1,132,728 |
| **LIABILITIES AND STOCKHOLDERS' EQUITY** | | |
| Current liabilities: | | |
| Accounts payable | $ 4,059 | $ 3,866 |
| Accrued expenses | 41,743 | 27,616 |
| Deferred revenue | 1,600 | 3,807 |
| Total current liabilities | 47,402 | 35,289 |
| Notes payable | 861,185 | 135,977 |
| Deferred rent | 3,162 | 2,853 |
| Other long-term liabilities | 4,747 | 2,130 |
| Total liabilities | 916,496 | 176,249 |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Convertible preferred stock, $.001 par value | | |
| Common stock, $.0005 par value | 77 | 76 |
| Additional paid-in capital | 905,886 | 840,232 |
| Accumulated other comprehensive income | 3,391 | 1,085 |
| Retained earnings | 218,582 | 115,086 |
| | 1,127,936 | 956,479 |
| Less treasury stock, at cost | 135,000 | |
| Total stockholders' equity | 992,936 | 956,479 |
| | $ 1,909,432 | $ 1,132,728 |

See accompanying notes to the condensed consolidated financial statements.



**IDEC PHARMACEUTICALS CORPORATION AND SUBSIDIARIES**

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

**(In thousands)**

**(unaudited)**

| | Nine months ended September 30, | |
|---|---|---|
| | **2002** | **2001** |

| | Nine months ended September 30, | |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income | $ 103,496 | $ 72,917 |
| Depreciation and amortization | 7,286 | 4,437 |
| Non-cash interest expense | 17,749 | 3,735 |
| Deferred rent | 309 | 100 |
| Deferred revenue | (2,207) | (4,144) |
| Deferred income taxes | 54,807 | 44,017 |
| Gain on sales of securities available-for-sale | (1,969) | (813) |
| Change in assets and liabilities: | | |
| Accounts receivable | (10,357) | 1,927 |
| Due from related parties, net | (17,037) | (20,711) |
| Inventories | (23,184) | (230) |
| Prepaid expenses and other assets | (14,844) | (1,658) |
| Restricted cash | (17,498) | |
| Accounts payable and accrued expenses | 15,878 | 3,160 |
| Other long-term liabilities | 791 | 522 |
| Net cash provided by operating activities | 113,220 | 103,259 |
| Cash flows from investing activities: | | |
| Purchases of property and equipment | (101,515) | (49,903) |
| Purchases of securities available-for-sale | (1,164,667) | (470,536) |
| Sales and maturities of securities available-for-sale | 552,321 | 433,688 |
| Net cash used in investing activities | (713,861) | (86,751) |
| Cash flows from financing activities: | | |
| Payments on notes payable | | (743) |
| Proceeds from notes payable, net of issuance costs | 696,004 | |
| Proceeds from issuance of common stock | 16,403 | 24,110 |
| Purchase of common stock for treasury | (135,000) | |
| Net cash provided by financing activities | 577,407 | 23,367 |
| Net (decrease) increase in cash and cash equivalents | (23,234) | 39,875 |
| Cash and cash equivalents, beginning of period | 425,999 | 401,052 |
| Cash and cash equivalents, end of period | $ 402,765 | $ 440,927 |

See accompanying notes to the condensed consolidated financial statements.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(In thousands, except per share data, percentages and unless as otherwise noted)**

**(Unaudited)**

**Note 1. Summary of Significant Accounting Policies**

*General:* The condensed consolidated financial statements as of September 30, 2002, and for the three and nine months ended September 30, 2002 and 2001 are unaudited. We have condensed or omitted certain information and footnote disclosures normally included in financial statements presented in accordance with accounting principles generally accepted in the United States of America. We believe the disclosures made are adequate to make the information presented not misleading. However, you should read these condensed consolidated financial statements in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2001.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Ultimate results could differ from those estimates. Interim results are not necessarily indicative of results for a full year or for any subsequent interim period.

In the opinion of management, these condensed consolidated financial statements include all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of results for the interim periods presented. Certain amounts in 2001 have been reclassified to conform to the 2002 presentation.

*Product Sales:* Product sales consist solely of sales of ZEVALIN®, our radioimmunotherapy product which was approved by the FDA for the treatment of certain B-cell non-Hodgkin's lymphomas, or NHLs, in February 2002. We have retained all United States marketing and distribution rights to ZEVALIN and have granted marketing and distribution rights outside the United States to Schering Aktiengesellschaft, or Schering AG. We recognize revenue from ZEVALIN product sales upon shipment. We record allowances for estimated uncollectible accounts receivable, product returns and Medicaid rebates at the time of sale.

**Note 2. Revenues from Unconsolidated Joint Business**

In March 1995, we entered into a collaborative agreement for the clinical development and commercialization of our anti-CD20 monoclonal antibody, Rituxan, for the treatment of certain B-cell NHLs with Genentech, Inc., or Genentech. Concurrent with the collaborative agreement we also entered into an expression technology license agreement with Genentech for a proprietary gene expression technology developed by us, and a preferred stock purchase agreement providing for certain equity investments in us by Genentech. Under the terms of these agreements, we will be reimbursed by Genentech for certain other development and regulatory approval expenses. Genentech may terminate this agreement for any reason, which would result in a loss of Genentech's Rituxan product rights.

In addition, we are copromoting Rituxan in the United States with Genentech under a joint business arrangement whereby we receive a share of the pretax copromotion profits. In September 1999, we transferred all worldwide manufacturing responsibilities for bulk Rituxan to Genentech.



Under the terms of separate agreements with Genentech, commercialization of Rituxan outside the United States is the responsibility of F. Hoffman-La Roche Ltd., or Roche, except in Japan where Roche continues development and copromotes Rituxan in collaboration with Zenyaku Kogyo Co. Ltd. We receive royalties on Rituxan sales outside the United States.

Revenues from unconsolidated joint business for the three and nine months ended September 30, 2002 and 2001 consist of the following:

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2002 | 2001 | 2002 | 2001 |

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| Copromotion profits | $ 82,924 | $ 62,836 | $ 226,060 | $ 159,034 |
| Reimbursement of selling and development expenses | 3,863 | 1,953 | 11,247 | 6,453 |
| Royalty income on sales of Rituxan outside the United States | 11,826 | 3,736 | 31,943 | 9,668 |
| Total revenues from unconsolidated joint business | $ 98,613 | $ 68,525 | $ 269,250 | $ 175,155 |

Amounts due from related parties, net at September 30, 2002 and December 31, 2001 primarily consist of amounts due from Genentech under our joint business arrangement.

**Note 3. Inventories**

Inventories are stated at the lower of cost, determined by the first-in, first-out method, or market. Inventories consist of the following:

| | September 30, 2002 | December 31, 2001 |
|---|---|---|
| Raw materials | $ 242 | $ 524 |
| Work in process | 23,294 | |
| Finished goods | 172 | |
| | $ 23,708 | $ 524 |

Pre-launch production of ZEVALIN antibodies manufactured prior to FDA approval in February 2002 were recognized as research and development expenses.

**Note 4. Earnings Per Share**

Earnings per share is calculated in accordance with Statement of Financial Accounting Standards No. 128, "Earnings per Share." Basic earnings per share utilizes net income and excludes the dilutive effects of stock options and other convertible securities. Diluted earnings per share utilizes net income adjusted for the after-tax amount of interest associated with convertible debt, and includes the potential dilutive effects of stock options and other convertible securities that could share in our earnings.



Calculations of basic and diluted earnings per share use the weighted-average number of shares outstanding during the period.

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2002 | 2001 | 2002 | 2001 |
| Numerator: | | | | |
| Net income | $ 38,440 | $ 26,957 | $ 103,496 | $ 72,917 |
| Adjustments for interest, net of income tax effect | 1,255 | | 3,732 | 3,434 |
| Net income, adjusted | $ 39,695 | $ 26,957 | $ 107,228 | $ 76,351 |

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| Denominator: | | | | |
| Weighted-average common shares outstanding | 152,679 | 152,061 | 152,977 | 150,142 |
| Effect of dilutive securities: | | | | |
| Stock options | 8,867 | 12,452 | 10,301 | 13,670 |
| Convertible preferred stock | 2,881 | 2,881 | 2,881 | 3,527 |
| Convertible promissory notes due 2019 | 13,935 | | 13,937 | 13,939 |
| Dilutive potential common shares | 25,683 | 15,333 | 27,119 | 31,136 |
| Weighted-average common shares and dilutive potential common shares | 178,362 | 167,394 | 180,096 | 181,278 |
| Basic earnings per share | $ 0.25 | $ 0.18 | $ 0.68 | $ 0.49 |
| Diluted earnings per share | $ 0.22 | $ 0.16 | $ 0.60 | $ 0.42 |

Excluded from the calculation of diluted earnings per share for the three and nine months ended September 30, 2002 were 8.7 million shares and 5.0 million shares, respectively, of common stock from the assumed conversion of our 30-year senior convertible promissory notes due 2032, and options to acquire 8.6 million shares and 5.3 million shares, respectively, of common stock because their effect would be antidilutive.

Excluded from the calculation of diluted earnings per share for the three months ended September 30, 2001 were 13.9 million shares of common stock from the assumed conversion of our subordinated convertible promissory notes due 2019, and options to acquire 2.9 million shares of common stock because their effect would be antidilutive. Excluded from the calculation of diluted earnings per share for the nine months ended September 30, 2001 were options to acquire 2.4 million shares of common stock because their effect would be antidilutive.

**Note 5. Comprehensive Income**

Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes certain changes in stockholders' equity that are excluded from net income, specifically, unrealized holding gains and losses on securities available-for-sale, net of tax. Total comprehensive income for the three months ended September 30, 2002 and 2001 was $40.2 million and $28.0 million, respectively. Total comprehensive income for the nine months ended September 30, 2002 and 2001 was $105.8 million and $74.3 million, respectively.



**Note 6. Segment Information**

We operate in one segment, which is the research, development, manufacture and commercialization of targeted therapies for the treatment of cancer and autoimmune and inflammatory diseases. The chief operating decision-makers review our operating results on an aggregate basis and manage our operations as a single operating segment.

**Note 7. Notes Payable**

In April and May 2002, we issued 30-year senior convertible promissory notes, or senior notes, for gross proceeds of approximately $714.4 million, or $696.0 million net of underwriting commissions and expenses of $18.4 million. Simultaneously with the issuance of the senior notes, we used a portion of the proceeds to fund the repurchase of $135.0 million of our outstanding common stock. The senior notes are zero coupon and were priced with a yield to maturity of 1.75% annually. We will pay contingent cash interest to the holders of these senior notes during any six-month period commencing on or after April 30, 2007 if the average market price of the senior notes for a five-trading-day measurement period preceding such six-month period equals 120% or more of the sum of the issue price and accrued original issue discount for such senior note. The contingent interest payable per senior note in respect of any quarterly period within such six-month period where contingent interest is determined to be payable will equal the greater of (1) the amount of regular cash dividends paid by us per share on our common stock during that quarterly period multiplied by the then applicable conversion rate or (2) 0.0625% of the average market price of a senior note for the five-trading-day measurement period preceding such six-month period, provided that if we do not pay regular cash dividends

during a semiannual period, we will pay contingent interest semiannually at a rate of 0.125% of the average market price of a senior note for the five-trading-day measurement period immediately preceding such six-month period.

Upon maturity, the senior notes will have an aggregate principal face value of $1.2 billion. Each $1,000 aggregate principal face value senior note is convertible at the holder's option at any time through maturity into 7.1881 shares of our common stock at an initial conversion price of $82.49. In addition, holders of the senior notes may require us to purchase all or a portion of the senior notes on April 29, 2005, 2007, 2012 and 2017 at a price equal to the issue price plus the accrued original issue discount to the date of purchase, payable at our option in cash, our common stock or a combination thereof. In addition, if a change in control in our company occurs on or before April 29, 2007, holders may require us to purchase all or a portion of their senior notes for cash. We have the right to redeem all or a portion of the senior notes for cash at any time on or after April 29, 2007 at set prices.

**Note 8. Contingencies**

On September 10, 2001, we filed a complaint against GlaxoSmithKline, plc, or Glaxo, and another complaint against Corixa Corporation, or Corixa, Coulter Pharmaceutical, Inc., or Coulter, and the Regents of the University of Michigan, in federal court for the Southern District of California. We are seeking declaratory judgment that ZEVALIN does not infringe patents held by the defendants and/or that the patents are invalid. On September 12, 2001, Corixa, Coulter and Glaxo filed a lawsuit against us in federal court in the district of Delaware alleging that ZEVALIN infringes their patents. This action has been transferred to the federal court for the Southern District of California and has been



consolidated with our lawsuit. Corixa's lawsuit against us seeks damages and to permanently enjoin us from selling ZEVALIN.

In addition, we are involved in certain other legal proceedings generally incidental to our normal business activities, which we believe will not have a material adverse effect on our business or financial condition.

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

**OVERVIEW**

We are primarily engaged in the research, development, manufacture and commercialization of targeted therapies for the treatment of cancer and autoimmune and inflammatory diseases.

In February 2002, ZEVALIN became the first radioimmunotherapy approved by the Food and Drug Administration, or FDA, for the treatment of certain B-cell NHLs. We have retained all United States marketing and distribution rights to ZEVALIN and have granted marketing and distribution rights outside the United States to Schering AG. In July 2002, we announced that marketing approval in Europe and European launch of ZEVALIN would be delayed. In October 2002, the Centers for Medicare and Medicaid Services, or CMS, informed us that the previously assigned C-codes and billing rate for the ZEVALIN therapeutic regimen became effective on October 1, 2002. In November 2002, CMS assigned a fixed reimbursement rate under which they will reimburse hospitals for the ZEVALIN therapeutic regimen for 2003.

Our other product, Rituxan, is being copromoted in the United States under a joint business arrangement with Genentech, where we receive a share of the pretax copromotion profits. Under the copromotion arrangement we share responsibility with Genentech for selling and continued development of Rituxan in the United States. Continued development of Rituxan includes conducting supportive research on Rituxan, post-approval clinical studies and obtaining approval of Rituxan for potential additional indications. Genentech provides the support functions for the commercialization of Rituxan in the United States including marketing, customer service, order entry, distribution, shipping and billing. Since September 1999, Genentech has been responsible for all worldwide manufacturing. Under the terms of separate agreements with Genentech, commercialization of Rituxan outside the United States is the responsibility of Roche, except in Japan where Roche continues development and copromotes Rituxan in collaboration with Zenyaku. We receive royalties on Rituxan sales outside the United States.

Our revenues include revenues from product sales of ZEVALIN, unconsolidated joint business revenues and corporate partner revenues. Until the commercialization of Rituxan, a substantial portion of our revenues had been derived from corporate partner revenues. However, since the commercialization of Rituxan in November 1997, our revenues have depended primarily upon the sale of Rituxan.

We have incurred increasing annual operating expenses and with the commercialization of Rituxan and ZEVALIN, we expect these trends to continue. From our inception in 1985, through 1997, we incurred annual operating losses. Our ongoing profitability will be dependent upon

the continued commercial success of Rituxan, the commercial success of ZEVALIN, product development and



revenues from the achievement of product development objectives and licensing transactions. As of September 30, 2002, we had retained earnings of $218.6 million.

**CRITICAL ACCOUNTING PRINCIPLES AND ESTIMATES**

The preparation of our condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires our management to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On a periodic basis, we evaluate our estimates, including those related to revenue recognition, allowance for doubtful accounts, inventory allowances, accounting for income taxes including the related valuation allowance, accruals for compensation and related benefits, and contingencies and litigation. These estimates are based on the information that is currently available and on various other assumptions that are believed to be reasonable under the circumstances. Actual results could vary from those estimates under different assumptions or conditions.

We have identified the following critical accounting policies that affect our more significant judgments and estimates used in the preparation of our condensed consolidated financial statements.

*Revenue recognition:* Revenues from unconsolidated joint business include our share of the pretax copromotion profits generated from our copromotion arrangement with Genentech, reimbursement from Genentech of our Rituxan-related sales force and development expenses and royalty revenue from Roche and Zenyaku on sales of Rituxan outside the United States. We record our royalty revenue from Roche and Zenyaku with a one-quarter lag. Under the copromotion arrangement, all U.S. sales of Rituxan and associated costs and expenses are recognized by Genentech and we record our share of the pretax copromotion profits on a quarterly basis, as defined in our collaborative agreement with Genentech. Pretax copromotion profits under the copromotion arrangement are derived by taking United States net sales of Rituxan to third-party customers less cost of sales, third-party royalty expenses, distribution, selling and marketing expenses and joint development expenses incurred by Genentech and us. Our profit-sharing formula with Genentech has two tiers; we earn a higher percentage of the pretax copromotion profits at the upper tier once a fixed pretax copromotion profit level is met. The profit-sharing formula resets annually at the beginning of each year to the lower tier. We began recording our profit share at the higher percentage during the first quarter of 2002 and 2001.

Corporate partner revenues consist of contract revenues and license fees. Contract revenues include nonrefundable research and development funding under collaborative agreements with our corporate partners and other funding under contractual arrangements with other parties. Contract research and development funding generally compensates us for discovery, preclinical and clinical expenses related to our collaborative development programs for our products and is recognized as research and development activities are performed under the terms of the collaborative agreements.

License fees includes nonrefundable fees from the sale of product rights and nonrefundable fees from product development milestone payments under collaborative development and license agreements with our corporate partners. Nonrefundable up-front fees from the sale of product rights are recorded as deferred revenue upon receipt and recognized as revenue over future periods as required by Securities and Exchange Commission's Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements," or SAB No. 101. Nonrefundable product development milestone



payments are recognized upon the achievement of product development milestone objectives as stipulated in agreements with our corporate partners. Product development milestone objectives vary in each of our agreements. The achievement of product development milestone objectives that may lead to the recognition of license fee revenues include:

- the achievement of preclinical research and development objectives;

the initiation of various phases of clinical trials;

the filing of an Investigational New Drug application, or IND, Biological License Application, or BLA, or New Drug Application, or NDA;

the filing of drug license applications in foreign territories; and

obtaining United States or foreign regulatory product approvals.

We recognize revenue from ZEVALIN product sales upon shipment. We record allowances for estimated uncollectible accounts receivable, product returns and Medicaid rebates at the time of sale.

*Accounting for income taxes:* As part of the process of preparing our condensed consolidated financial statements we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves us estimating our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items, such as deferred revenue, for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our condensed consolidated balance sheet. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income and, to the extent we believe that recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase this allowance in a period, we may include an expense within the income tax provision in the statement of operations.

Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. We have recorded a valuation allowance of $66.5 million and $70.7 million, respectively, as of September 30, 2002 and December 31, 2002 due to uncertainties related to our ability to utilize some of our deferred tax assets, primarily consisting of certain net operating loss carryforwards, before they expire. The valuation allowance is based on our estimates of taxable income by jurisdiction in which we operate and the period over which our deferred tax assets will be recoverable. Our estimates of taxable income are derived from, among other items, our estimates of deductions related to stock options. In the event that actual results differ from these estimates or we adjust these estimates in future periods, we may need to adjust our valuation allowance which could materially impact our financial position and results of operations. Our net deferred tax asset as of September 30, 2002 and December 31, 2001 was $60.5 million and $67.0 million, respectively, net of the valuation allowance.

**RECENT DEVELOPMENTS**

On September 5, 2002, we announced the completion of a preliminary review of the clinical results of our two Phase II clinical trials of IDEC-114 for patients with moderate-to-severe psoriasis, and that the data did not support further development in this indication. We continue to develop IDEC-114 in non-Hodgkin's lymphoma.



On September 30, 2002, we announced the retirement of Phillip M. Schneider, Senior Vice Presdient and Chief Financial Officer, to pursue personal and community interests.

**RESULTS OF OPERATIONS**

Revenues from unconsolidated joint business for the three and nine months ended September 30, 2002 and 2001, consist of the following:

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2002 | 2001 | 2002 | 2001 |
| Copromotion profits | $ 82,924 | $ 62,836 | $ 226,060 | $ 159,034 |
| Reimbursement of selling and development expenses | 3,863 | 1,953 | 11,247 | 6,453 |
| | 11,826 | 3,736 | 31,943 | 9,668 |

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| Royalty income on sales of Rituxan outside the United States | | | | |
| Total revenues from unconsolidated joint business | $ 98,613 | $ 68,525 | $ 269,250 | $ 175,155 |

Under our agreement with Genentech, our pretax copromotion profit-sharing formula has two tiers. We earn a higher percentage of the pretax copromotion profits at the upper tier once a fixed pretax copromotion profit level is met. The profit-sharing formula resets annually at the beginning of each year to the lower tier. We began recording our profit share at the higher percentage during the first quarter of 2002 and 2001.

Rituxan net sales to third-party customers in the United States recorded by Genentech for the three and nine months ended September 30, 2002 amounted to $269.6 million and $762.0 million, respectively, compared to $205.0 million and $553.0 million for the comparable periods in 2001. This increase was primarily due to increased market penetration in treatments of B-cell non-Hodgkin's lymphoma and an increase in the wholesale price of Rituxan effective on March 1, 2002.

Our royalty revenue on sales of Rituxan outside the United States is based on Roche and Zenyaku's end-user sales and is recorded with a one-quarter lag. For the three and nine months ended September 30, 2002, we recognized $11.8 million and $31.9 million, respectively, in royalties from Roche and Zenyaku's end-users sales compared to $3.7 million and $9.7 million for the comparable periods in 2001. The increase in royalty revenue for the three months and nine months ended September 30, 2002 is primarily due to higher sales of Rituxan outside the United States resulting from increased penetration of foreign markets, including initial sales of Rituxan in Canada and Japan.

Corporate partner revenues for the three months ended September 30, 2002 totaled $0.1 million compared to $1.1 million for the comparable period in 2001. The decrease in corporate partner revenues for the three months ended September 30, 2002 is primarily the result of decreased funding under our collaborative agreements with Eisai Co., Ltd. and Schering AG and termination of our collaborative agreement with Taisho Pharmaceuticals Co. Ltd. of Tokyo. Corporate partner revenues for the nine months ended September 30, 2002 totaled $3.1 million compared to $15.8 million for the comparable period in 2001. The decrease in corporate partner revenues for the nine months ended September 30, 2002 is primarily the result of decreased funding under our collaborative agreements



with Taisho, Eisai and Schering AG, and, during the nine months ended September 30, 2001, the recognition of a $5.0 million milestone payment from Schering AG when the European Medicines Evaluation Agency accepted for filing the submission of a Marketing Authorization, or MAA, for the approval of ZEVALIN in Europe, and $1.6 million in upfront license fees received from Schering AG in 1999 resulting from our adoption of SAB No. 101.

Corporate partner revenues may vary from period to period and are, in part, dependent upon achievement of certain research and development objectives or the consummation of new corporate alliances. The magnitude and timing of corporate partner revenues may influence our level of profitability. For example, the delay in ZEVALIN approval in Europe will result in a delay in the payment and recognition of a $10.0 million product approval milestone from Schering AG.

Product sales were $5.0 million and $8.3 million, respectively, for the three and nine months ended September 30, 2002 and consist solely of net sales of ZEVALIN in the United States. We have retained all United States marketing and distribution rights for ZEVALIN. Cost of sales as a percentage of product sales was 5% and 14%, respectively, for the three and nine months ended September 30, 2002 and primarily consists of contractual royalties owed on ZEVALIN sales and manufacturing variances. Pre-launch production of ZEVALIN antibodies manufactured prior to FDA approval in February 2002 were recognized as research and development expenses. ZEVALIN sales to date have solely consisted of ZEVALIN antibodies produced prior to FDA approval in February 2002. Had pre-launch production of ZEVALIN antibodies been capitalized as inventory, cost of sales as a percentage of product sales for the three and nine months ended September 30, 2002 would have been approximately 8% and 17%, respectively.

Research and development expenses totaled $25.4 million and $67.6 million for the three and nine months ended September 30, 2002, respectively, compared to $20.8 million and $63.9 million for the comparable periods in 2001. The increase in research and development expenses for the three and nine months ended September 30, 2002 is primarily due to upfront fees totaling $4.5 million incurred under new collaborations, increased personnel expenses and expansion of our facilities to support our ongoing basic research and clinical development programs, offset by capitalization of manufacturing costs for the production of commercial inventory of ZEVALIN antibodies and decreased

clinical testing and development costs for ZEVALIN as a result of the FDA's approval of ZEVALIN. In the future we expect to continue incurring substantial additional research and development expenses due to:

- preclinical and clinical testing of our various products under development;
- the expansion or addition of research and development programs;
- technology in-licensing;
- regulatory-related expenses;
- the expansion of clinical manufacturing capabilities; and
- facilities expansion.

Selling, general and administrative expenses totaled $23.8 million and $65.9 million for the three and nine months ended September 30, 2002, respectively, compared to $13.0 million and $36.1 million for the comparable periods in 2001. This increase is primarily due to increased marketing and administrative expenses related to the commercialization of ZEVALIN, sales expenses to support the



commercialization of Rituxan, legal settlement costs and outside legal counsel fees to protect our intellectual property rights for ZEVALIN and general increases in general and administrative expenses to support overall organizational growth. Selling, general and administrative expenses are expected to increase in the foreseeable future to support the following:

- marketing and administration related to the commercialization of ZEVALIN;
- manufacturing capacity expansion;
- clinical trials;
- research and development; and
- protection and enforcement of our intellectual property rights for ZEVALIN and our product candidates.

Interest income totaled $9.9 million and $24.3 million for the three and nine months ended September 30, 2002, respectively, compared to $8.8 million and $30.5 million for the comparable periods in 2001. The increase in interest income for the three months ended September 30, 2002 is primarily due to higher cash balances from the issuance of our senior notes in April 2002. The decrease in interest income for the nine months ended September 30, 2002 is primarily due to lower interest rates realized on our cash, cash equivalents and securities available-for-sale partially offset by higher cash balances from the issuance of our senior notes in April 2002.

Interest expense totaled $5.1 million and $11.1 million for the three and nine months ended September 30, 2002, respectively, compared to $1.8 million and $5.5 million for the comparable periods in 2001. This increase is primarily due to additional non-cash interest expense from our senior notes issued in April 2002.

Our effective tax rate for the three and nine months ended September 30, 2002 was approximately thirty-five percent compared to approximately thirty-seven percent for the comparable periods in 2001. This decrease in our effective tax rate in 2002 is primarily due to an

increase in our research and experimentation credits and orphan drug credit. Our net operating loss carryforwards available to offset future taxable income at December 31, 2001 were approximately $174.0 million for federal income tax purposes and begin to expire in 2009. The utilization of our net operating loss carryforwards and tax credits may be subject to an annual limitation under the Internal Revenue Code due to a cumulative change of ownership of more than 50% in prior years. However, we anticipate this annual limitation to result only in a slight deferral in the utilization of our net operating loss carryforwards and tax credits. We expect that our effective tax rate in the future will continue to approximate the maximum statutory tax rate.

**LIQUIDITY AND CAPITAL RESOURCES**

We have financed our operating and capital expenditures since inception principally through the sales of equity securities, profits from our copromotion arrangement with Genentech related to the sale of Rituxan, corporate partner revenues, lease financing transactions, debt financing transactions and interest income. We expect to finance our current and planned operating requirements principally through cash on hand, which includes proceeds from the April 2002 issuance of our senior notes, anticipated funds from our copromotion arrangement with Genentech, commercial sales of ZEVALIN



and with funds from existing collaborative agreements and contracts. We believe that these funds will be sufficient to meet our operating requirements for the foreseeable future. Existing collaborative research agreements and contracts, however, could be canceled by the contracting parties. In addition, we may from time to time seek additional funding through a combination of new collaborative agreements, strategic alliances and additional equity and debt financings or from other sources. Additional funds may not be obtainable through these sources on acceptable terms, if at all. If adequate funds are not obtainable from the copromotion arrangement, operations or additional sources of financing, our business could be harmed. Our working capital and capital requirements will depend upon numerous factors, including:

- the continued commercial success of Rituxan;
- the commercial success of ZEVALIN;
- timing and expense of obtaining regulatory approvals;
- funding and timing of payments related to several material capital projects;
- financing alternatives available for the construction of our large-scale manufacturing facilities and corporate headquarters and research and development campus;
- the progress of our preclinical and clinical testing;
- fluctuating or increasing manufacturing requirements and research and development programs;
- levels of resources that we devote to the development of manufacturing, sales and marketing capabilities, including resources devoted to the marketing of ZEVALIN;
- technological advances;
- status of competitors;

our ability to establish collaborative arrangements with other organizations; and

working capital required to satisfy the put options related to our senior notes.

Until required for operations, we invest our cash reserves in bank deposits, certificates of deposit, commercial paper, corporate notes, foreign and United States government instruments and other readily marketable debt instruments in accordance with our investment policy.

At September 30, 2002, we had $1.5 billion in cash, cash equivalents and securities available-for-sale compared to $866.6 million at December 31, 2001. Sources of cash during the nine months ended September 30, 2002, included $696.0 million from the issuance of our senior notes, $113.2 million from operations and $16.4 million from the issuance of common stock under employee stock option and purchase plans. Uses of cash during the nine months ended September 30, 2002 included the net increase in our securities available-for-sale portfolio of $612.3 million, $135.0 million for the repurchase of our common stock for treasury and $101.5 million to fund construction projects and purchase capital equipment.

In April and May 2002, we raised through the issuance of our senior notes, approximately $696.0 million, net of underwriting commissions and expenses of $18.4 million. Simultaneously with the issuance of the senior notes, we used a portion of the proceeds to fund the repurchase of



$135.0 million of our outstanding common stock. The senior notes are zero coupon and were priced with a yield to maturity of 1.75% annually. We will pay contingent cash interest to the holders of these senior notes during any nine-month period commencing on or after April 30, 2007 if the average market price of the senior notes for a five-trading-day measurement period preceding such nine-month period equals 120% or more of the sum of the issue price and accrued original issue discount for such senior note. The contingent interest payable per senior note in respect of any quarterly period within such nine-month period where contingent interest is determined to be payable will equal the greater of (1) the amount of regular cash dividends paid by us per share on our common stock during that quarterly period multiplied by the then applicable conversion rate or (2) 0.0625% of the average market price of a senior note for the five-trading-day measurement period preceding such nine-month period, provided that if we do not pay regular cash dividends during a semiannual period, we will pay contingent interest semiannually at a rate of 0.125% of the average market price of a senior note for the five-trading-day measurement period immediately preceding such nine-month period.

Upon maturity, the senior notes will have an aggregate principal face value of $1.2 billion. Each $1,000 aggregate principal face value senior note is convertible at the holder's option at any time through maturity into 7.1881 shares of our common stock at an initial conversion price of $82.49. In addition, holders of the senior notes may require us to purchase all or a portion of the senior notes on April 29, 2005, 2007, 2012 and 2017 at a price equal to the issue price plus the accrued original issue discount to the date of purchase, payable at our option in cash, our common stock or a combination thereof. In addition, if a change in control in our company occurs on or before April 29, 2007, holders may require us to purchase all or a portion of their senior notes for cash. We have the right to redeem all or a portion of the senior notes for cash at any time on or after April 29, 2007 at set prices.

Under the terms of our agreement with MDS Canada, Inc., we are obligated to make periodic payments into an escrow account. These funds secure certain obligations we have under our agreement regarding minimum annual purchases and MDS Canada, Inc.'s establishment of a new facility to supply us with Yttrium-90. In general, our required escrow deposits will decrease over time if certain Yttrium-90 minimum annual purchase commitments are met. As of September 30, 2002, we have paid $22.5 million into this escrow fund.

In September 2001, we purchased approximately 42.6 acres in San Diego for approximately $31.7 million in cash for a proposed corporate headquarters and research and development campus. The first phase of construction is expected to be completed in mid 2004 at an estimated total cost of $177 million to be funded from our working capital. As of September 30, 2002, we have invested approximately $4.6 million towards the construction of this campus.

In April 2001, we purchased a 43,000 square foot facility in Oceanside to house our future clinical manufacturing area. Construction is expected to be completed in the fourth quarter of 2002 at an estimated total cost of $57 million to be funded from our working capital. As of September 30, 2002, we have invested approximately $34.0 million towards construction of this clinical manufacturing facility.

In September 2000, we purchased a 60-acre site in Oceanside for approximately $18.9 million in cash. We plan to build a large-scale manufacturing facility at the location, which we anticipate using to commercialize our products currently in clinical trials if they are approved by the FDA. This expansion will allow us to better control the manufacture of our products, reducing our reliance on contract

manufacturers, as well as to reduce commercial risk. We expect the first phase of the new facility to be mechanically completed in 2004, followed by commissioning and validation in 2005 and 2006. Estimated total costs of this facility upon completion are $400 million to be funded from our working capital. As of September 30, 2002, we have invested approximately $58.7 million towards the construction of this large-scale manufacturing facility.

In February 1999, we raised through the sale of convertible promissory notes approximately $112.7 million, net of underwriting commissions and expenses of $3.9 million. The convertible promissory notes are zero coupons and were priced with a yield to maturity of 5.5 percent annually. Upon maturity, the convertible promissory notes will have an aggregate principal face value of $345.0 million. Each $1,000 aggregate principal face value convertible promissory note is convertible at the holders' option at any time through maturity into 40.404 shares of our common stock at an initial conversion price of $8.36. We are required under the terms of the convertible promissory notes, as of 35 business days after a change in control occurring on or before February 16, 2004, to purchase any convertible promissory note at the option of its holder at a price equal to the issue price plus accrued original issue discount to the date of purchase. Additionally, the holders of the convertible promissory notes may require us to purchase the convertible promissory notes on February 16, 2004, 2009 or 2014 at a price equal to the issue price plus accrued original issue discount to the date of purchase payable at our option in cash, our common stock or a combination thereof. We have the right to redeem the convertible promissory notes on or after February 16, 2004.

In connection with our research and development efforts, we have entered into various collaborative arrangements under which we may be obligated to pay royalties or milestone payments if product development is successful. It is not anticipated that the aggregate of any royalty or milestone obligations under these arrangements will be material to our operations.



## FORWARD-LOOKING INFORMATION AND RISK FACTORS THAT MAY AFFECT FUTURE RESULTS

*This Form 10-Q contains forward-looking statements based on our current expectations. These statements include, without limitation, statements about market opportunity, our growth and sale strategies and our expectations, plans and objectives. In some cases, you can identify these statements by terminology such as anticipate, believe, estimate, expect, intend, may, plan, should or will or similar phrases or expressions. You should be aware that these statements are projections or estimates as to future events, and actual results may differ materially.*

*In addition to the other information contained in this Form 10-Q, you should consider the following risk factors which could affect our actual future results and could harm our business, financial condition and results of operations. The risks and uncertainties described below are not the only risks facing us and additional risks and uncertainties may also harm our business.*

**Our Revenues Rely Significantly on Rituxan Sales.**

Our revenues currently depend substantially upon continued sales of Rituxan. For the year ended December 31, 2001, approximately 92 percent of our revenues were derived from our Rituxan copromotion arrangement with Genentech. For the nine-months ended September 30, 2002, 96 percent of our revenues were derived from our Rituxan copromotion arrangement with Genentech. We cannot assure you that Rituxan will continue to be accepted in the United States or in any foreign markets or that Rituxan sales will continue to increase. A number of factors may affect the rate and level of market acceptance of Rituxan, including:

- the perception by physicians and other members of the healthcare community of its safety and efficacy or that of competing products, if any;
- the effectiveness of our and Genentech's sales and marketing efforts in the United States and the effectiveness of Roche's sales and marketing efforts outside the United States and Japan;
- unfavorable publicity concerning Rituxan or similar drugs;

its price relative to other drugs or competing treatments;

the availability and level of third-party reimbursement; and

regulatory developments related to the manufacture or continued use of Rituxan.

Given our current reliance on Rituxan as the principal source of our revenue, any material adverse developments with respect to the commercialization of Rituxan may cause our revenue to decrease and may cause us to incur losses in the future.

**If We Fail to Commercialize ZEVALIN Successfully in the United States, to Obtain Marketing Approval for ZEVALIN in Europe or to Commercialize ZEVALIN Successfully in Europe, Our Business Will Be Harmed.**

Our radioimmunotherapy product ZEVALIN was approved by the FDA for marketing and sale in the United States in February 2002 and we began selling the product in April 2002. We cannot assure you that ZEVALIN will be accepted or widely used by physicians and other members of the healthcare



community in the United States. Further, marketing approval for ZEVALIN in Europe has been delayed due to compliance issues at our fill/finish provider and we cannot be certain that, even if marketing approval is obtained, our exclusive worldwide marketing partner, Schering AG, will be able to successfully commercialize ZEVALIN in Europe. Factors that might impact the successful commercialization of ZEVALIN include:

the perception by physicians and other members of the healthcare community of its safety and efficacy or that of competing products, if any;

unfavorable publicity concerning ZEVALIN or similar drugs;

its price relative to other drugs or competing treatments;

the availability and level of third-party reimbursement; and

regulatory developments related to the manufacture or continued use of ZEVALIN.

In addition, we have no marketing support service experience and, therefore, we are dependent on outside contractors to meet those needs for ZEVALIN. For example, we rely upon a third-party logistics distributor to provide customer service, order entry, shipping and billing. Customer reimbursement assistance is provided by a separate outside contractor. We cannot assure that the integration of these marketing support services can be successfully coordinated. Further, given our limited marketing and sales experience, we cannot assure you that we will be successful in selling ZEVALIN in the United States.

We rely on MDS Canada, Inc. to provide the market with the Yttrium-90 radioisotope required for therapeutic use of ZEVALIN, and we rely on third parties for various manufacturing steps of ZEVALIN. In addition, there are currently only two sources approved by the FDA to supply the Indium-111 isotope required for the imaging use of ZEVALIN. If we were to lose the services of any of these parties, we would be forced to find other providers, which could delay our ability to sell ZEVALIN. In addition, each of these third-party providers is subject to continuing inspection by the FDA or comparable agencies in other jurisdictions. A delay or an interruption in the manufacture of ZEVALIN or the production of the Yttrium-90 radioisotope for any reason, including as a result of a failure to pass any regulatory agency inspection, or an impairment of the commercial availability of Indium-111, could significantly impair our ability to sell ZEVALIN.

**We May Be Unable to Develop and Commercialize New Products.**

Our future results of operations depend to a large extent upon our ability to successfully develop and commercialize new products in a timely and competitive manner. As a result, we must continue to develop, test and manufacture new products and then must meet regulatory standards and obtain regulatory approvals for any new products. Our products currently in development may not receive the regulatory approvals from the FDA or comparable agencies in other jurisdictions necessary for marketing in a timely manner, if at all. Failure to receive such approval would preclude us from marketing any such drugs in the United States or such other jurisdictions. Additionally, the development and commercialization process is time-consuming and costly, and we cannot assure you that any of our products, if and when developed and approved, will be successfully commercialized or competitive in the marketplace. Delays or unanticipated costs in any part of the process or our inability to obtain regulatory approval for our products, to effectively commercialize our products, or to



maintain manufacturing facilities in compliance with all applicable regulatory requirements could harm our business.

**We Have Limited Manufacturing Experience and Rely Heavily on Contract Manufacturers.**

We rely heavily upon third-party manufacturers to manufacture significant portions of Rituxan, ZEVALIN and our product candidates. Our current manufacturing capacity is limited. Our manufacturing experience to date has been limited to the production of preclinical and clinical quantities of product candidates, approximately three years of commercial production of bulk Rituxan and portions of our commercial requirements of the bulk antibody for ZEVALIN. We have no fill/finish experience or capacity, and we do not have experience manufacturing in the field of chelates or radioisotopes, which are required for our production of ZEVALIN. Therefore, we rely entirely upon third parties for fill/finish services as well as the manufacture of most of our product components. Consequently, we cannot assure you that either our manufacturing facilities or our ability to sustain ongoing production of our products will be able to meet our expectations. If our current third-party manufacturers or service providers fail to meet our expectations, we may not be able to enter into satisfactory agreements with other third party manufacturers or service providers. Poor performance or coordination on our part or that of our third-party manufacturers or service providers could harm our business.

ZEVALIN has multiple components that require successful coordination among ourselves and several third-party contract manufacturers and suppliers. We may not be able to integrate and coordinate successfully our contract manufacturers and suppliers. In addition, our contract manufacturers and suppliers are required to maintain compliance with current Good Manufacturing Practices, or cGMP, and are subject to inspections by the FDA or comparable agencies in other jurisdictions to confirm this compliance. Any changes of suppliers or modifications of methods of manufacturing require amending our application to the FDA and ultimate amendment acceptance by the FDA prior to release of product to the market place. Their inability to demonstrate ongoing cGMP compliance and produce ZEVALIN components could interrupt commercial supply of ZEVALIN. For example, our current third-party manufacturer for ZEVALIN remains subject to a warning letter from the FDA with respect to cGMP matters not specifically related to ZEVALIN. A manufacturer subject to a warning letter that fails to correct cGMP deficiencies to the satisfaction of the FDA could be subject to interruption of production pending resolution of the cGMP issues. Further, we are working with our current third-party manufacturer to address issues related to the manufacture of commercial quantities of ZEVALIN. If ZEVALIN production was interrupted or our third-party manufacturer was unable to manufacture adequate commercial quantities of ZEVALIN in a timely manner, it could adversely affect our results of operations.

We rely on Genentech for all Rituxan manufacturing to meet worldwide requirements. We cannot ensure that Genentech will manufacture and fill/finish Rituxan in sufficient quantities and on a timely and cost-effective basis or that Genentech will obtain and maintain all required manufacturing approvals. Genentech's failure to manufacture and fill/finish Rituxan or obtain and maintain required manufacturing approvals could harm our business.

In addition, we converted our current manufacturing facility to a multi-product facility. From this facility, we have manufactured and will continue to manufacture our own commercial requirements of the bulk antibody and other kit components for ZEVALIN. We cannot assure you that our



manufacturing performance will meet our expectations. Our inability to maintain regulatory approval of our manufacturing facility for ZEVALIN would harm our ability to timely produce commercial supplies of the ZEVALIN antibody. To the extent we cannot produce our own biologics, we will need to rely on third-party manufacturers, of which there are only a limited number capable of manufacturing biologics products as contract suppliers. We cannot be certain that we could reach agreement on reasonable terms, if at all, with those manufacturers.

**We Rely Heavily on a Limited Number of Suppliers.**

Some materials used in Rituxan, ZEVALIN and our product candidates are currently available only from a single supplier or a limited number of suppliers. Some of these suppliers are subject to ongoing FDA approvals or other governmental regulations. Any interruption or delay in our supply of materials required to sell our products could harm our business if we were unable to obtain an alternative supplier for these materials in a cost-effective and timely manner. Additional factors that could cause interruptions or delays in our source of materials include limitations on the availability of raw materials or manufacturing performance experienced by our suppliers and a breakdown in our commercial relations with one or more suppliers. These factors may be completely out of our control.

For example, we have entered into an agreement with MDS Canada, Inc., the commercial supplier of the Yttrium-90 radioisotope for ZEVALIN, and will rely upon them to supply our clinical and commercial requirements. If MDS Canada, Inc. does not maintain FDA approvals or approvals of comparable agencies in other jurisdictions to produce the radioisotope Yttrium-90 for ZEVALIN, or if we are unable to receive an adequate supply of this radioisotope for any other reason, including those described above, we would be unable to sell ZEVALIN for therapeutic use unless we were to obtain a new supplier. We are aware of other entities that may be able to provide the radioisotope that we need for the therapeutic use of ZEVALIN but we believe that these suppliers would be required to apply for additional governmental approvals to do so. The process of establishing a relationship with another supplier and the process of obtaining the required governmental approvals would be time consuming and uncertain. We cannot assure you that we could reach an agreement with another supplier in a timely manner or on commercially reasonable terms, if at all. As a result of these concerns, if we were to lose our supply or were unable to receive sufficient quantities of the radioisotope from our sole supplier, our ability to sell ZEVALIN could be harmed which, in turn, could significantly harm our business.

**We Have Limited Sales and Marketing Experience.**

We have limited experience with commercial sales and marketing, based entirely upon our launch and subsequent sales of Rituxan. ZEVALIN is our first product to be marketed exclusively by us in the United States. Outside the United States, our strategy for future products is to pursue and to rely solely upon collaborations with established pharmaceutical companies for marketing, distribution and sale of our products. We currently have no plans to directly market either of our products outside the United States. Given that we rely on Genentech to copromote Rituxan with us in the United States and rely exclusively on third parties to market Rituxan and ZEVALIN outside the United States, we cannot be certain that our products will be marketed and distributed in accordance with our expectations or that our market research or sales forecasts will be accurate. We have no marketing support service experience and, therefore, we will be dependent on outside contractors to meet those



needs. We rely upon a third-party logistics distributor to provide customer service, order entry, shipping and billing. Customer reimbursement assistance is provided by a separate outside contractor. We cannot assure you that the integration of these marketing support services can be successfully coordinated. Neither can we assure you that we will ever be able to develop our own marketing and sales capabilities to an extent that we would not need to rely on third-party efforts, or that we will be able to maintain satisfactory arrangements with the third parties on whom we rely.

**Our Operating Results Are Subject to Significant Fluctuations.**

Our quarterly revenues, expenses and operating results have fluctuated in the past and are likely to fluctuate significantly in the future. Fluctuation may result from a variety of factors, including:

- our achievement of product development objectives and milestones;
- demand and pricing for Rituxan and ZEVALIN;
- timing and nature of contract manufacturing and contract research and development payments and receipts;
- hospital and pharmacy buying decisions;

clinical trial enrollment and expenses;

research and development and manufacturing expenses;

percent of time that our manufacturing facilities are utilized for commercial or clinical support;

expenses related to protecting our intellectual property;

physician acceptance of our products;

government or private healthcare reimbursement policies;

our manufacturing performance and capacity and that of our partners;

amount and timing of sales orders for Rituxan by Genentech for customers in the United States and by Roche for customers outside the United States and Japan;

amount and timing of our sales orders for ZEVALIN for customers in the United States and, if approved in Europe, by Schering AG for customers outside the United States;

rate and success of product approvals;

timing of regulatory approval, if any, of competitive products and the rate of market penetration of competing products;

collaboration obligations and copromotion payments we make or receive;

interest rate fluctuations;

foreign currency exchange rates; and

overall economic conditions.



Our operating results during any one quarter do not necessarily suggest the anticipated results of future quarters. These results fluctuate periodically because our revenues are driven by the occurrence of events, for example, the achievement of product development milestones and the applicable profit sharing allocations between us and our marketing partners Genentech and Schering AG.

**We Are Subject to Uncertainties Regarding Healthcare Reimbursement and Reform.**

Our ability to commercialize products depends in part on the extent to which patients are reimbursed by governmental agencies, private health insurers and other organizations, such as health maintenance organizations, for the cost of such products and related treatments. Our business could be harmed if healthcare payers and providers implement cost-containment measures and governmental agencies implement healthcare reform. In addition, we cannot assure you that current or any future level of Medicare reimbursement for our products will be viewed favorably by health care providers and that they will prescribe our products as a result. If health care providers are unable to receive reimbursement at a level that they deem to be sufficient, our results of operations could be adversely affected.

**We Face Uncertain Results of Clinical Trials of Our Potential Products.**

Our future success depends in large part upon the results of clinical trials designed to assess the safety and efficacy of our potential products. The completion rate of clinical trials depends significantly upon the rate of patient enrollment. Our inability to enroll patients on a timely basis could result in increased expenses and product development delays, which could harm our business. We cannot assure you that patients enrolled in our clinical trials will respond to our product candidates, that any product candidate will be safe and effective or that data derived from the trials will be suitable for submission to the FDA or satisfactorily support a BLA, sBLA or NDA. Factors that affect patient enrollment include:

- size of patient population for the targeted disease;
- eligibility criteria;
- proximity of eligible patients to clinical sites;
- clinical trial protocols; and
- the existence of competing protocols, including competitive financial incentives for patients and clinicians, and existing approved drugs, including Rituxan.

Even if a trial is fully enrolled, significant uncertainties remain as to whether it will prove successful. For example, in September 2002 we announced that we will not pursue further development of IDEC-114 for patients with moderate-to-severe psoriasis. In addition, we announced during the second quarter of 2002 that we had placed a voluntary hold on all ongoing clinical trials for our anti-CD40 ligand monoclonal antibody, IDEC-131. We cannot predict when, if ever, we will resume clinical trials on IDEC-131.

In addition, the length of time necessary to complete clinical trials and submit an application for marketing and manufacturing approvals varies significantly and may be difficult to predict. Failure to comply with extensive FDA regulations may result in delay, suspension or cancellation of a trial or the



FDA's refusal to accept test results. The FDA may also suspend our clinical trials at any time if it concludes that the participants are being exposed to unacceptable risks. Consequently, we cannot ensure that Phase I, Phase II, Phase III or Phase IV post-marketing testing will be completed timely or successfully, if at all, for any of our potential or existing products. Furthermore, success in preclinical and early clinical trials does not ensure that later phase or large-scale trials will be successful.

**Our Industry Is Intensely Competitive.**

The biotechnology industry is intensely competitive and we may not be able to produce or acquire rights to new products with commercial potential. We compete with biotechnology and pharmaceutical companies that have been established longer than we have, have a greater number of products on the market, have greater financial and other resources and have other technological or competitive advantages. We also compete in the development of technologies and processes and in acquiring personnel and technology from academic institutions, government agencies, and other private and public research organizations. We cannot be certain that one or more of our competitors will not receive patent protection that dominates, blocks or adversely affects our product development or business; will benefit from significantly greater sales and marketing capabilities; or will not develop products that are accepted more widely than ours.

One of our competitors, Corixa Corporation, formerly Coulter Pharmaceuticals, or Corixa, is pursuing FDA approval for BEXXAR® (tositumomab, iodine I-131 tositumomab), an investigational radioimmunotherapy for the treatment of low-grade or transformed low-grade NHL. We are aware that Corixa received a Complete Review Letter from the FDA indicating that Corixa has not demonstrated that BEXXAR provides sufficient evidence of safety and net clinical benefit of BEXXAR for it to be approved. Corixa was granted an appeal of the FDA's position. As a result, Corixa has been granted an opportunity to present data on BEXXAR at the December 17, 2002 Oncologic Drugs Advisory Committee, or ODAC, meeting. If Corixa is successful at the ODAC meeting and is able to provide sufficient evidence to the FDA to support

FDA approval for BEXXAR, our business could be adversely affected.

We are also aware of other potentially competitive biologic therapies for non-Hodgkin's lymphoma in development.

**We May Be Unable to Adequately Protect or Enforce Our Intellectual Property Rights or Secure Rights to Third-Party Patents and We Are Involved in Patent Litigation.**

Our ability and the abilities of our partners to obtain and maintain patent and other protection for our products will affect our ability to compete. We are assigned, have rights to, or have exclusive licenses to a number of U.S. and foreign patents and patent applications. However, the pending patent applications may not issue as patents and, even if approved, our patent rights may not be upheld by a court or may be narrowed if challenged. The patent positions of pharmaceutical and biotechnology companies can be highly uncertain and involve complex legal and factual questions. Our patent rights may not provide competitive advantages for our products and may be challenged, infringed upon or circumvented by our competitors.

In addition to patents, we rely on trade secrets and proprietary know-how that we seek to protect, in part, through confidentiality agreements with our partners, employees and consultants. These parties



may breach our agreements and courts may not enforce the agreements, leaving us without adequate remedies. Further, our trade secrets may become known or be developed independently or patented by our competitors.

If it were ultimately determined that our claimed intellectual property rights are unenforceable, or that our use of our products infringes the rights of others, we may be required or may desire to obtain licenses to patents and other intellectual property held by third parties to develop, manufacture and market our products. We may not be able to obtain these licenses on commercially reasonable terms, if at all, and any licensed patents or intellectual property that we may obtain may not be valid or enforceable. In addition, the scope of intellectual property protection is subject to scrutiny and challenge by courts and other governmental bodies. Litigation and other proceedings concerning patents and proprietary technologies can be protracted, expensive and distracting to management and companies may sue competitors as a way of delaying the introduction of competitors' products. Any litigation, including any interference proceedings to determine priority of inventions, oppositions to patents in foreign countries or litigation against our partners, may be costly and time consuming and could harm our business.

Because of the large number of patent filings in the biopharmaceutical field, our competitors may have filed applications or been issued patents and may obtain additional patents and proprietary rights relating to products or processes competitive with or similar to ours. We cannot be certain that U.S. or foreign patents do not exist or will not issue that would harm our ability to commercialize our products and product candidates.

**Patent Litigation Related to Rituxan**

On May 28, 1999 and September 14, 2000, Glaxo filed two patent infringement lawsuits against Genentech. These suits assert that the manufacture, use, and sale of Rituxan infringes U.S. patents owned by Glaxo. The trial for the first of these suits concluded on May 4, 2001 with the jury unanimously finding that Rituxan does not infringe patents held by Glaxo. The jury also unanimously found that all of the patent claims that Glaxo asserted against Genentech were invalid. Glaxo has appealed this ruling with respect to a subset of the asserted patents. The judge has rescheduled the trial for the second suit to begin in late 2002. To date we have not been named in either of these suits. If Glaxo were to prevail in the second suit or on appeal of the first suit, it could be awarded a variety of remedies, including damages for past sales, requiring Genentech to obtain a license from Glaxo or obtaining an injunction against the sale of Rituxan. Because we rely on sales of Rituxan for substantially all of our revenue, an injunction would significantly harm our business. Further, if Genentech were required to obtain a license from Glaxo, our operating results in a particular quarter could be harmed as a result of any payment required for past royalties. Additionally, our long-term profitability could be harmed by reduced profit sharing under our collaboration agreement with Genentech as a result of future royalties and other payments to Glaxo.

Glaxo has also sued Roche in Germany asserting that Rituxan infringes Glaxo's patents. On October 26, 2000, a German court handling the infringement phase of the suit issued a decision holding that the manufacture, use and sale of Rituxan infringes patents held by Glaxo. Roche has appealed the decision and the appeal is pending before the Court of Appeals. At the end of 2001, a German court handling the validity phase of the trial held that the three patents were invalid. Additionally, Roche has filed oppositions in the European Patent Office, or EPO, to several of the

Glaxo patents. Although we were not named in the suit, if Glaxo obtains an injunction precluding further sale of Rituxan in Europe, our business could be harmed.

**Patent Litigation Related to ZEVALIN**

On September 10, 2001, we filed a complaint against GlaxoSmithKline, plc, or Glaxo, and another complaint against Corixa Corporation, or Corixa, Coulter Pharmaceutical, Inc., or Coulter, and the Regents of the University of Michigan, in federal court for the Southern District of California. We are seeking declaratory judgment that ZEVALIN does not infringe patents held by the defendants and/or that the patents are invalid. On September 12, 2001, Corixa, Coulter and Glaxo filed a lawsuit against us in federal court in the district of Delaware alleging that ZEVALIN infringes their patents. This action has been transferred to the federal court for the Southern District of California and has been consolidated with our lawsuit. Corixa's lawsuit against us seeks damages and to permanently enjoin us from selling ZEVALIN. We cannot predict or determine the outcome of this litigation. An unfavorable outcome could limit our ability to sell ZEVALIN, could require us to pay damages for past sales of ZEVALIN and could require that we obtain a license from third parties to sell ZEVALIN. Any such unfavorable outcome could harm our business and our results of operations.

**Proceedings Related to Anti-CD40L Antibodies**

In September 1999, an interference to determine priority of inventorship was declared in the United States Patent and Trademark Office, or USPTO, between Dartmouth University's patent application, which has been exclusively licensed to us, and Columbia University's patent, which we believe has been exclusively licensed to Biogen, Inc., relating to anti-CD40L antibodies. In October 2001, the USPTO issued a decision concluding that there was no interference between the Dartmouth application and the Columbia patent. We appealed the decision to the Court of Appeals, Federal Circuit in December 2001. If the decision of the USPTO is upheld, the Columbia patent will remain in force and could be asserted against us.

We, along with other companies, have filed oppositions to a Japanese patent assigned to Immunex Corporation relating to anti-CD40L antibodies. We are also aware that oppositions have been filed in the EPO to granted European applications that have been licensed to us. Each of these applications contain claims relating to the use of anti-CD40L antibodies as a therapeutic. Also, we are aware of an opposition that has been filed to a granted European patent application which names us as the applicant and which relates to PROVAX and therapeutic use thereof. This opposition has been heard by the Oppositions Division of the EPO. The claims of the European patent covering PROVAX were narrowed, yet are still of sufficient scope to cover the PROVAX product. If the outcome of any of the oppositions is adverse, in whole or in part, it could result in the scope of some or all of the granted claims being limited, some or all of the granted claims being lost, the granted patent application not proceeding to a patent or our competitors having patent claims that may be asserted against us.

**Potential Conflicts with Third-Party Patent Rights**

We are aware of several third-party patents and patent applications, to the extent they issue as patents, that if successfully asserted against us may adversely affect our ability to make, use, offer to sell, sell and import our products. These third-party patents and patent applications may include a



number of U.S. and foreign patents that relate to various aspects of our products and product candidates.

The owners, or licensees of the owners of these patents, or any foreign patents, and patent applications, to the extent they issue as patents, may assert that one or more of our products infringe one or more claims of these patents. If legal action is commenced against us or our partners to enforce any of these patents and patent applications, to the extent they issue as patents, and the plaintiff in such action prevails, we could be prevented from practicing the subject matter claimed in such patents.

**Failure to Obtain Product Approvals or Comply with Government Regulations Could Harm Our Business.**

As pharmaceutical companies, we and our partners, contract manufacturers and suppliers are subject to rigorous and extensive regulation by governmental authorities in the United States and other countries. In the United States, our products cannot be marketed until they are approved by the FDA. Obtaining FDA approval involves the submission, among other information, of the results of preclinical and clinical studies on the

product and requires substantial time, effort and financial resources. The FDA will also conduct prelicensing inspections of the facility or facilities at which the product is manufactured to determine compliance with cGMP. Rituxan and ZEVALIN are our only products that have received FDA approval, and we cannot assure you that our product candidates will be approved either in the United States or in other countries in a timely fashion, if at all. Failure to comply with FDA requirements, both before and after product approval, may subject us and/or our partners, contract manufacturers and suppliers to administrative or judicial sanctions, including FDA refusal to approve pending applications, warning letters, product recalls, product seizures, total or partial suspension of production or distribution, fines, injunctions and/or criminal prosecution.

**We May Be Unable to Maintain Third-Party Research and Development Relationships.**

Funding of research and development efforts depends largely upon various arrangements with corporate partners and others who provide us with funding and who perform research and development with respect to our products. These corporate partners may generally terminate their arrangements with us at any time. These parties may develop products that compete with ours, and we cannot be certain that they will perform their contractual obligations or that any revenues will be derived from such arrangements. If one or more of our corporate partners fail to achieve product development objectives, this failure could harm our ability to fund related programs and develop products.

**Our Business Exposes Us to Product Liability Claims.**

Our design, testing, development, manufacture and marketing of products involve an inherent risk of exposure to product liability claims and related adverse publicity. Insurance coverage is expensive and difficult to obtain, and we may be unable to obtain coverage in the future on acceptable terms, if at all. Although we currently maintain product liability insurance for our products in the amounts we believe to be commercially reasonable, we cannot be certain that the coverage limits of our insurance policies or those of our strategic partners will be adequate. If we are unable to obtain sufficient insurance at an acceptable cost or if a successful product liability claim is made against us, whether fully covered by insurance or not, our business could be harmed.



**We May Not Be Able to Successfully Develop and Commence Operations of Our New Manufacturing and Clinical Facilities.**

We purchased a 60-acre parcel of land and a 43,000 square foot building on adjacent property in Oceanside, California on which we intend to develop manufacturing and clinical facilities. We have limited experience in developing these types of facilities and may not be able to successfully develop or commence operations at these facilities. If we fail to successfully develop or commence operations at these new facilities, we may be unable to commercialize or meet demands for future products, if any. We may encounter difficulties in designing, constructing and initiating our manufacturing facilities, including:

- governmental regulation of our manufacturing facility, specifically, FDA or comparable agency approvals required for the commercial manufacture of our product candidates currently in clinical trials;
- public opinion regarding the impact of the facility on nearby communities;
- construction delays, including obtaining necessary governmental approvals and permits;
- cost overruns;
- delays in design, shipment and installation of equipment for our facility;
- natural disasters;
- other unforeseeable factors inherent in the construction process; and

obtaining financing we may need to complete the facility.

Even if we are able to successfully develop this manufacturing facility, we may not be able to do so in a cost-effective manner or in a time frame that is consistent with our expected future manufacturing needs or our future manufacturing needs may not be sufficient to allow the facility to be fully operational, which could harm our business.

**Our Business Involves Environmental Risks.**

Our business and the business of several of our strategic partners, including Genentech, involve the controlled use of hazardous materials, chemicals, biologics and radioactive compounds. Biologics manufacturing is extremely susceptible to product loss due to microbial or viral contamination, material equipment failure, or vendor or operator error. Although we believe that our safety procedures for handling and disposing of such materials complies with state and federal standards, there will always be the risk of accidental contamination or injury. In addition, microbial or viral contamination may cause the closure of a manufacturing facility for an extended period of time. By law, radioactive materials may only be disposed of at state-approved facilities. We currently store our radioactive materials on-site because the approval of a disposal site in California for all California-based companies has been delayed indefinitely. If and when a disposal site is approved, we may incur substantial costs related to the disposal of these materials. If we were to become liable for an accident, or if we were to suffer an extended facility shutdown, we could incur significant costs, damages and penalties that could harm our business.



**We Rely Upon Key Personnel.**

Our success will depend, to a great extent, upon the experience, abilities and continued services of our executive officers and key scientific personnel. If we lose the services of any of these officers or key scientific personnel, our business could be harmed. Our success also will depend upon our ability to attract and retain other highly qualified scientific, managerial, sales and manufacturing personnel and our ability to develop and maintain relationships with qualified clinical researchers. Competition for these personnel and relationships is intense and we compete with numerous pharmaceutical and biotechnology companies as well as with universities and non-profit research organizations. We may not be able to continue to attract and retain qualified personnel or develop and maintain relationships with clinical researchers.

**Future Transactions May Harm Our Business or the Market Price of Our Securities.**

We regularly review potential transactions related to technologies, products or product rights and businesses complementary to our business. These transactions could include:

mergers;

acquisitions;

strategic alliances;

off-balance sheet financings;

licensing agreements; and

copromotion agreements.

We may choose to enter into one or more of these transactions at any time, which may cause substantial fluctuations to the market price of securities that we have issued. Moreover, depending upon the nature of any transaction, we may experience a charge to earnings, which could also harm the market price of securities that we have issued.

**Volatility of Our Stock Price.**

The market prices for our common stock and for securities of other companies engaged primarily in biotechnology and pharmaceutical development, manufacture and distribution are highly volatile. For example, the market price of our common stock fluctuated between $20.76 per share and $71.40 per share during the nine months ended September 30, 2002. The market price of our common stock likely will continue to fluctuate due to a variety of factors, including:

material public announcements;

the announcement and timing of new product introductions by us or others;

technical innovations or product development by us or our competitors;

regulatory approvals or regulatory issues;

availability and level of third-party reimbursement;

developments relating to patents, proprietary rights and orphan drug status;



actual or potential clinical results with respect to our products under development or those of our competitors;

political developments or proposed legislation in the pharmaceutical or healthcare industry;

economic and other external factors, disaster or crisis;

hedge and/or arbitrage activities by holders of our convertible promissory notes;

period-to-period fluctuations in our financial results or results which do not meet or exceed analyst expectations; and

market trends relating to or affecting stock prices throughout our industry, whether or not related to results or news regarding us or our competitors.

**We May Be Unable to Raise Additional Capital.**

We expend and will likely continue to expend substantial funds to complete the research, development, manufacturing and marketing of our potential future products. Consequently, we may seek to raise capital through collaborative arrangements, strategic alliances or equity and debt financings or from other sources. We may need to raise additional funds or borrow funds to complete the construction of our planned facilities. We may be unable to raise additional capital on commercially acceptable terms, if at all, and if we raise capital through equity financing, existing stockholders may have their ownership interests diluted. Our failure to be able to generate adequate funds from operations or from additional sources would harm our business.

**Our Outstanding LYONs Leverage Us Considerably.**

As a result of issuing our LYONs due 2019 in February 1999 and issuing our LYONs due 2032 in April and May 2002, we incurred indebtedness of approximately $345.0 million at maturity in 2019 and approximately $1.2 billion at maturity in 2032. As a result of this indebtedness, our principal and interest obligations increased substantially. The degree to which we are leveraged could harm our ability to obtain future financing and could make us more vulnerable to industry downturns and competitive pressures. Our ability to meet our debt

obligations will be dependent upon our future performance, which will be subject to financial, business and other factors affecting our operations, many of which are beyond our control.

**We Have Adopted Several Anti-takeover Measures.**

We have taken a number of actions that could discourage a takeover attempt that might be beneficial to stockholders who wish to receive a premium for their shares from a potential bidder. For example:

- we reincorporated into Delaware, which subjects us to Section 203 of the Delaware General Corporation Law, providing that we may not enter into a business combination with an interested stockholder for a period of three years after the date of the transaction in which the person became an interested stockholder, unless the business combination is approved in the manner prescribed in the code section;



- we have adopted a stockholder rights plan that was amended and restated as of July 26, 2001 that would cause substantial dilution to a person who attempts to acquire us on terms not approved by our board of directors;

- our board of directors has the authority to issue, without vote or action of stockholders, up to 8,000,000 shares of preferred stock and to fix the price, rights, preferences and privileges of those shares. Any series of preferred stock could contain dividend rights, conversion rights, voting rights, terms of redemption, redemption prices, liquidation preferences or other rights superior to the rights of holders of common stock. Although we currently have 48,014 shares of non-voting convertible preferred stock outstanding, which were convertible into 2,880,840 shares of common stock as of December 31, 2001, the board of directors has no present intention of issuing any additional shares of preferred stock. However, the board of directors may issue additional series of preferred stock in the future;

- our copromotion arrangement with Genentech provides Genentech with the option to buy the rights to Rituxan in the event that we undergo a change of control or we introduce a competing product, which may limit our attractiveness to potential acquirors;

- under the terms of the LYONs any acquiror would be required to repurchase the LYONs for cash in connection with its acquisition of us before 2007; and

- our directors are elected to staggered terms, which prevents the entire board from being replaced in any single year.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

We are exposed to a variety of risks, including changes in interest rates affecting the return on our investments and the cost of our debt.

At September 30, 2002, we maintained a portion of our cash and cash equivalents in financial instruments with original maturities of three months or less. We also maintained an investment portfolio containing financial instruments in which the majority have original maturities of greater than three months but less than twenty-four months. These financial instruments, principally consisting of corporate obligations and to a lesser extent foreign and U.S. government obligations, are subject to interest rate risk and will decline in value if interest rates increase. A hypothetical ten percent change in interest rates during the nine months ended September 30, 2002, would have resulted in an approximately $2.3 million change in pretax income. We have not used derivative financial instruments in our investment portfolio.

Our long-term debt totaled $861.2 million at September 30, 2002 and consisted principally of our promissory notes issued in February 1999 and our senior notes issued in April 2002. These long-term debt obligations bear interest at a weighed average interest rate of 2.4%. Due to the fixed rate nature of our promissory and senior notes, an immediate ten percent change in interest rates would not have a material effect on our financial condition or results of operations.

Underlying market risk exists related to an increase in our stock price or an increase in interest rates may make conversion of the convertible promissory notes to common stock beneficial to the convertible promissory notes holder. Conversion of the convertible promissory notes would have a dilutive effect on our earnings per share and book value per common share.



**Item 4. Controls and Procedures.**

We performed an evaluation under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures within the 90-day period prior to filing of this report. Based on that evaluation, our management, including our principal executive officer and principal financial officer, concluded that our disclosure controls and procedures are effective and provide for timely collection and evaluation of information that may need to be disclosed to investors. There have been no significant changes in our internal controls or in other factors that could significantly affect these controls subsequent to the date of our evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.



**PART II OTHER INFORMATION**

**Item 6. Exhibits and Reports on Form 8-K.**

(a)

Exhibits referenced

| Exhibit Number | Description |
|---|---|
| 10.10 | Amended and Restated 1988 Stock Option Plan, as amended and restated through October 22, 2002. |
| 10.30 | Form of Stock Option Agreement. |

(b)

Reports on Form 8-K. On September 5, 2002, we filed a current report of Form 8-K reporting that we announced results of Phase II clinical trials of our IDEC-114 anti-CD80 monoclonal antibody for patients with moderate-to-severe psoriasis.



**Signatures**

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.

IDEC PHARMACEUTICALS CORPORATION

Date: November 14, 2002 By: /s/ WILLIAM H. RASTETTER

William H. Rastetter
*Chairman of the Board and*
*Chief Executive Officer*
*(Principal Executive Officer)*

Date: November 14, 2002 By: /s/ EDWARD M. RODRIGUEZ

Edward M. Rodriguez
*Vice President and Controller*
*(Principal Financial and Accounting Officer)*



**Certifications**

I, William H. Rastetter, certify that:

1. I have reviewed this quarterly report on Form 10-Q of IDEC PHARMACEUTICALS CORPORATION;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

   a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

   b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

   c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

   a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's

auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 14, 2002

/s/ WILLIAM H. RASTETTER

William H. Rastetter
*Chairman of the Board and*
*Chief Executive Officer*
*(Principal Executive Officer)*



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I, Edward M. Rodriguez, certify that:

1. I have reviewed this quarterly report on Form 10-Q of IDEC PHARMACEUTICALS CORPORATION;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 14, 2002

/s/ EDWARD M. RODRIGUEZ

Edward M. Rodriguez
*Vice President and Controller*
*(Principal Financial and Accounting Officer)*



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