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

FORM 10-Q

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

For the quarterly period ended September 30, 2003

or

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

For the transition period from _____ to _____

Commission File Number: 0-27488

INCYTE CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	**94-3136539**
(State or other jurisdiction of incorporation or organization)	**(IRS Employer Identification No.)**

3160 Porter Drive
Palo Alto, California 94304
(Address of principal executive offices)

(650) 855-0555
(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 ☐ No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

☒ Yes ☐ No

The number of outstanding shares of the registrant's Common Stock, $0.001 par value, was 72,456,424 as of October 31, 2003.

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PART I: FINANCIAL INFORMATION

Item 1: Financial Statements

INCYTE CORPORATION
Condensed Consolidated Balance Sheets
(in thousands)
(unaudited)

	September 30, 2003 (unaudited)	December 31, 2002 *
ASSETS		
Current assets:		
Cash and cash equivalents	$ 14,307	$ 22,928
Marketable securities—available-for-sale	300,791	406,090
Accounts receivable, net [1]	10,179	8,485
Prepaid expenses and other current assets [2]	12,557	21,268
Total current assets	337,834	458,771
Property and equipment, net	30,786	31,787
Long-term investments [3]	18,208	35,515
Intangible and other assets, net [4]	28,609	26,066
Total assets	$ 415,437	$ 552,139
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 7,157	$ 9,073
Accrued compensation	12,559	14,319
Accrued and other current liabilities [5]	6,840	11,043
Deferred revenue	8,922	11,662
Accrued restructuring charges	16,024	31,596
Accrued acquisition costs	1,980	—
Total current liabilities	53,482	77,693
Convertible subordinated notes	167,890	172,036
Total liabilities	221,372	249,729
Stockholders' equity:		
Common stock	72	67
Additional paid-in capital	726,113	708,163
Deferred compensation	(1,315)	(3,250)
Accumulated other comprehensive income (loss)	(85)	2,454
Accumulated deficit	(530,720)	(405,024)
Total stockholders' equity	194,065	302,410
Total liabilities and stockholders' equity	$ 415,437	$ 552,139

* The condensed consolidated balance sheet at December 31, 2002 has been derived from the audited financial statements at that date.

(1) Includes receivables from companies considered related parties under SFAS 57 of $0.2 million and $0.6 million at September 30, 2003 and December 31, 2002, respectively.

(2) Includes loan receivable from Maxia Pharmaceuticals, Inc. (see Note 12), a company considered a related party under SFAS 57 as of December 31, 2002, of $1.5 million at December 31, 2002, and prepaid expenses to companies considered related parties under SFAS 57 of $0 million and $2.1 million at September 30, 2003 and December 31, 2002, respectively.

(3) Includes investments in companies considered related parties under SFAS 57 of $16.6 million and $29.1 million at September 30, 2003 and December 31, 2002, respectively.

(4) Includes loans to executive officers of $0.2 million and $0.8 million, net of amortization, at September 30, 2003 and December 31, 2002, respectively.

(5) Includes accruals of payments to companies considered related parties under SFAS 57 of $0 million and $1.5 million at September 30, 2003 and December 31, 2002, respectively.

See accompanying notes

INCYTE CORPORATION
Condensed Consolidated Statements of Operations
(in thousands, except per share amounts)
(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Revenues [1]	$ 13,249	$ 22,390	$ 36,794	$ 80,463
Costs and expenses:				
Research and development [2]	28,619	47,406	88,675	118,761
Selling, general and administrative [3]	8,585	12,147	23,656	39,063
Purchased in-process research and development	6,250	—	34,366	—
Loss on sale of assets	—	9	—	114
Other expenses	(35)	292	1,358	1,663
Total costs and expenses	43,419	59,854	148,055	159,601
Loss from operations	(30,170)	(37,464)	(111,261)	(79,138)
Interest and other income (expense), net [4]	(11,259)	1,648	(7,536)	16,406
Interest expense	(2,299)	(2,450)	(7,177)	(7,377)
Gain on repurchase of convertible subordinated notes	706	—	706	1,937
Gain (loss) on certain derivative financial instruments, net	200	155	263	(318)
Loss before income taxes	(42,822)	(38,111)	(125,005)	(68,490)
Provision for income taxes	190	300	691	903
Net loss	$ (43,012)	$ (38,411)	$ (125,696)	$ (69,393)
Basic and diluted net loss per share:	$ (0.60)	$ (0.57)	$ (1.77)	$ (1.03)
Shares used in computing basic and diluted net loss per share	72,185	67,740	71,022	67,348

(1) Includes revenues from transactions with companies considered related parties under SFAS 57 of $0.2 million and $0.2 million for the three months ended September 30, 2003 and 2002, respectively, and revenues of $0.6 million and $1.4 million for the nine months ended September 30, 2003 and 2002, respectively.

(2) Includes expenses from transactions with companies considered related parties under SFAS 57 of $1.0 million and $5.1 million for the three months ended September 30, 2003 and 2002, respectively, and expenses of $2.1 million and $10.6 million for the nine months ended September 30, 2003 and 2002, respectively.

(3) Includes compensation expense related to loans to executive officers of $0.1 million and $0 million for the three months ended September 30, 2003 and 2002, respectively, and $0.2 million and $0 million for the nine months ended September 30, 2003 and 2002, respectively.

(4) Includes loss on long-term investments in companies considered related parties under SFAS 57 of $12.5 million and $0 million for the three months ended September 30, 2003, and 2002, respectively, and loss on long-term investments of $12.5 million and a gain on long-term investments of $0.8 million for the nine months ended September 30, 2003 and 2002, respectively.

See accompanying notes

INCYTE CORPORATION
Condensed Consolidated Statements of Comprehensive Loss
(in thousands)
(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Net loss	$ (43,012)	$ (38,411)	$ (125,696)	$ (69,393)
Other comprehensive income (loss):				
Unrealized gains (losses) on marketable securities	(631)	2,257	(2,484)	(9,490)
Foreign currency translation adjustments	(25)	12	(55)	(236)
Other comprehensive income (loss)	(656)	2,269	(2,539)	(9,726)
Comprehensive loss	$ (43,668)	$ (36,142)	$ (128,235)	$ (79,119)

See accompanying notes

INCYTE CORPORATION
Condensed Consolidated Statements of Cash Flows
(in thousands)
(unaudited)

	Nine Months Ended September 30,	
	2003	2002
Cash flows from operating activities:		
Net loss	$ (125,696)	$ (69,393)
Adjustments to reconcile net loss to net cash used in operating activities:		
Non-cash other expenses	393	—
Non-cash purchased in-process research and development	28,116	—
Depreciation and amortization	13,443	16,863
Gain on repurchase of convertible subordinated notes	(706)	(1,937)
Compensation expense on executive loans	227	—
Stock compensation	1,285	3,409
(Gain) loss on derivative financial instruments, net	(263)	318
Realized gain on long-term investments, net	(1,265)	(1,064)
Loss on sale of assets	—	114
Impairment of long-term investments	16,064	408
Impairment of prepaid and other assets	—	8,100
Equity received in exchange for goods or services provided	—	(2,688)
Changes in certain assets and liabilities:		
Accounts receivable, net	(1,694)	39,258
Prepaid expenses and other assets	(493)	(6,373)
Accounts payable	(2,724)	(131)
Accrued and other current liabilities	(22,320)	(17,019)
Deferred revenue	(2,740)	(8,529)
Net cash used in operating activities	(98,373)	(38,664)
Cash flows from investing activities:		
Acquisition of Maxia Pharmaceuticals, net of cash acquired	(5,126)	—
Purchase of long-term investments	—	(5,000)
Proceeds from the sale of long-term investments	2,647	2,637
Capital expenditures	(8,696)	(10,487)
Purchases of marketable securities	(504,846)	(573,410)
Sales and maturities of marketable securities	607,784	597,379
Loans to executive officers	—	(1,150)
Net cash provided by investing activities	91,763	9,969
Cash flows from financing activities:		
Proceeds from issuance of common stock under stock plans	1,208	5,916
Repurchase of common stock	(105)	—
Repurchase of convertible subordinated notes	(3,059)	(4,690)
Other	—	73
Net cash (used in) provided by financing activities	(1,956)	1,299
Effect of exchange rate on cash and cash equivalents	(55)	(236)
Net decrease in cash and cash equivalents	(8,621)	(27,632)
Cash and cash equivalents at beginning of period	22,928	43,368
Cash and cash equivalents at end of period	$ 14,307	$ 15,736

See accompanying notes

INCYTE CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2003
(Unaudited)

1. Organization and business

Incyte Corporation ("Incyte", "we", "us" or "our"), formerly Incyte Genomics, Inc., was incorporated in Delaware in April 1991. In March 2003, we changed our name to Incyte Corporation. Incyte is a drug discovery company that is using its expertise in medicinal chemistry and molecular, cellular and in vivo biology to discover and develop novel therapeutics. We believe we have the largest compilation of information regarding full-length human genes and the proteins they encode and the largest commercial portfolio of issued United States patents covering such genes and proteins. We use this intellectual property in our drug discovery programs and also license this intellectual property, as well as market and license our genomic and proteomic information, to many of the world's leading pharmaceutical and biotechnology companies and academic research centers. Incyte has also assembled an experienced and talented drug discovery team that is identifying potential new drug therapies for cancer, inflammatory diseases and other medical conditions. Incyte has also in-licensed a compound for treatment of human immunodeficiency virus ("HIV") that is currently in clinical development.

2. Summary of significant accounting policies

Basis of presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. The condensed consolidated balance sheet as of September 30, 2003, condensed consolidated statements of operations for the three and nine months ended September 30, 2003 and 2002, condensed consolidated statements of comprehensive loss for the three and nine months ended September 30, 2003 and 2002 and the condensed consolidated statements of cash flows for the nine months ended September 30, 2003 and 2002 are unaudited, but include all adjustments which the Company considers necessary for a fair presentation of the financial position, operating results and cash flows for the periods presented. The balance sheet at December 31, 2002 has been derived from audited financial statements.

Although we believe that the disclosures in these financial statements are adequate to make the information presented not misleading, certain information and footnote information normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission.

Results for any interim period are not necessarily indicative of results for any future interim period or for the entire year. The accompanying financial statements should be read in conjunction with the financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2002.

Stock-based compensation

In accordance with the provisions of FASB Statement No. 123, *Accounting for Stock-Based Compensation ("SFAS 123")*, Incyte has elected to continue applying the provisions of APB Opinion No. 25, *Accounting for Stock Issued to Employees ("APB 25")*, as amended by FASB Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation ("FIN 44")*, in accounting for our stock-based compensation plans. Accordingly, we do not recognize compensation expense for stock options granted to employees and directors when the stock option price at the grant date is equal to or greater than the fair market value of the stock at that date.

The fair value of each option and employee purchase right was estimated at the date of grant using a Black-Scholes option-pricing model, assuming no expected dividends and the following weighted average assumptions:

	Employee Stock Options				Employee Stock Purchase Plan			
	For the Three Months Ended September 30,		For the Nine Months Ended September 30,		For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2003	2002	2003	2002	2003	2002	2003	2002
Average risk-free interest rates	2.22%	2.69%	2.78%	3.62%	1.75%	1.53%	1.59%	1.87%
Average expected life (in years)	3.41	3.36	3.41	3.48	2.00	0.50	1.31	0.50
Volatility	92%	88%	92%	87%	93%	108%	100%	95%

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because our employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of our employee stock options.

For purposes of disclosures pursuant to SFAS 123, as amended by FASB Statement No. 148, *Accounting for Stock-Based Compensation – Transition and Disclosure* ("SFAS 148"), the estimated fair value of options is amortized over the options' vesting period. The following illustrates the pro forma effect on net loss and net loss per share as if we had applied the fair value recognition provisions of SFAS 123 (in thousands, except per share amounts):

	For the Three Months Ended September 30		For the Nine Months Ended September 30	
	2003	2002	2003	2002
Net loss, as reported	$(43,012)	$(38,411)	$(125,696)	$(69,393)
Add: Stock-based employee compensation	286	1,081	1,285	3,409
Deduct: Total stock-based employee compensation determined under the fair value-based method for all awards	(4,198)	(6,534)	(9,777)	(18,604)
Pro forma net loss	$(46,924)	$(43,864)	$(134,188)	$(84,588)
Net loss per share:				
Basic and diluted net loss per share-as reported	$ (0.60)	$ (0.57)	$ (1.77)	$ (1.03)
Basic and diluted net loss per share-as SFAS 123 adjusted	$ (0.65)	$ (0.65)	$ (1.89)	$ (1.26)

We also record, and amortize over the related vesting periods, deferred compensation representing the difference between the price per share of stock issued or the exercise price of stock options granted and the fair value of our common stock at the time of issuance or grant.

3. Property and equipment

Property and equipment consisted of (in thousands):

	September 30, 2003	December 31, 2002
Office equipment	$ 4,513	$ 4,968
Laboratory equipment	25,616	24,489
Computer equipment	63,286	70,817
Leasehold improvements	31,168	31,010
	124,583	131,284
Less accumulated depreciation and amortization	(93,797)	(99,497)
	$ 30,786	$ 31,787

4. Long-term investments

We have made equity and debt investments in a number of companies whose businesses may be complementary to our business; most of these investments were made in connection with the establishment of a collaborative arrangement between us and the investee company. We account for our investments in publicly-traded companies in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. These investments are classified as available-for-sale and are adjusted to their fair value each period based on their traded market price with any adjustments being recorded in accumulated other comprehensive income (loss) as a separate component of stockholders' equity. Investments in privately-held companies are carried at cost. We own less than 20% of the outstanding voting stock of each long-term investment and do not have the ability to exert significant influence over these investments.

Investment impairment charges are recorded when we believe that an investment has experienced a decline in value that is other than temporary. The determination of whether an impairment is other than temporary consists of a review of qualitative and quantitative factors by members of senior management. Generally, declines that persist for six months or more are considered

other than temporary. We use the best information available in these assessments; however, the information available may be limited. These determinations involve significant management judgment, and actual amounts realized for any specific investment may differ from the recorded values. Future adverse changes in market conditions or poor operating results of underlying investments could result in additional impairment charges

As of September 30, 2003, our long-term investments consisted of equity investments in privately-held companies. For the three and nine months ended September 30, 2003, we recorded an impairment charge of $13.4 million and $16.1 million, respectively, as a result of writedowns related to reduced market valuations of our long-term investments. Impairment charges are included in “Interest and other income (expense), net.”

One long-term investment comprised 14% and 42% of the total long-term investments balance at September 30, 2003 and December 31, 2002, respectively. The activity in our long-term investments, in any given quarter, may result in gains or losses on sales or impairment charges. Amounts realized upon disposition of these investments may be different from their carrying value.

5. Intangible and other assets

Intangible and other assets, net, totaling $28.6 million and $26.1 million at September 30, 2003 and December 31, 2002, respectively, consisted of $24.1 million and $20.1 million of intangible assets, net, at September 30, 2003 and December 31, 2002, respectively, and $4.5 million and $6.0 million of other assets at September 30, 2003 and December 31, 2002, respectively. Intangible assets consisted of the following (in thousands):

	September 30, 2003			December 31, 2002		
	Gross Carrying Amount	Accumulated Amortization	Other Intangibles, Net	Gross Carrying Amount	Accumulated Amortization	Other Intangibles, Net
Capitalized patents	$ 19,943	$ (2,936)	$ 17,007	$ 14,465	$ (1,582)	$ 12,883
Capitalized software	9,652	(4,570)	5,082	7,638	(2,797)	4,841
Acquired database technology	2,638	(705)	1,933	2,638	(429)	2,209
Other intangibles	362	(280)	82	362	(171)	191
Total	$ 32,595	$ (8,491)	$ 24,104	$ 25,103	$ (4,979)	$ 20,124

Costs of patents and patent applications are capitalized and amortized on a straight-line basis over their estimated useful lives of approximately ten years in accordance with the provisions of Accounting Principles Board Opinion No. 17, *Intangible Assets (“APB 17”)*. Capitalized software costs, which consist of software development costs incurred in developing certain products once the technological feasibility of the products has been determined, are recorded in accordance with FASB Statement No. 86, *Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed (“SFAS 86”)*, and are amortized on a straight-line basis over the estimated useful life of three years. Acquired database technology and other intangible assets recorded in conjunction with the acquisition of Proteome, Inc. are being amortized using the straight-line method over estimated useful lives ranging from three to eight years. Amortization expense related to intangibles was $1.3 million and $3.6 million for the three and nine months ended September 30, 2003, respectively, and $1.0 million and $2.7 million for the three and nine months ended September 30, 2002.

6. Convertible subordinated notes

In February 2000, in a private placement, Incyte issued $200.0 million of convertible subordinated notes, which resulted in net proceeds of approximately $196.8 million. The notes bear interest at 5.5%, payable semi-annually on February 1 and August 1, and are due February 1, 2007. The notes are subordinated to all senior indebtedness, as defined. The notes can be converted at the option of the holder at an initial conversion price of $67.42 per share, subject to adjustment. We may, at our option, redeem the notes at any time at specific prices. Holders may require us to repurchase the notes upon a change in control, as defined.

During the three and nine month periods ended September 30, 2003, we repurchased on the open market and retired $3.8 million in face value of convertible subordinated notes and recognized a gain of $0.7 million. During the three and nine month periods ended September 30, 2002, we repurchased on the open market and retired $0 million and $6.7 million in face value of convertible subordinated notes, respectively. A gain of $0 million and $1.9 million was recognized on these transactions for the three and nine months ended September 30, 2002, respectively. All gains on repurchase of convertible subordinated notes are presented as “Gain on repurchase of convertible subordinated notes.”

7. Revenue recognition

Revenues are recognized when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed and determinable and collectibility is reasonably assured. We enter into various types of agreements

for access to our databases of information, use of our intellectual property and sales of our custom products and services. Revenue is deferred for fees received before earned or until no further obligations exist.

Revenues received from agreements in which collaborators paid with equity securities in their company were $0 million for both the three and nine months ended September 30, 2003, respectively, and $0 million and $2.4 million for the three and nine months ended September 30, 2002, respectively. Additionally, revenues received from agreements in which we concurrently invested funds in the collaborator's equity securities were $0.2 million and $0.6 million for the three and nine months ended September 30, 2003, respectively, and $0.2 million and $0.6 million for the corresponding periods in 2002.

Revenues recognized from transactions in which there was originally a concurrent commitment entered into by us to purchase goods or services for the three and nine months ended September 30, 2003 were $0.8 million and $2.7 million, respectively. No new transactions in which there was a concurrent commitment by us to purchase goods or services were entered into during the three and nine months ended September 30, 2003. Of commitments made in prior periods, we expensed $2.8 million and $8.3 million for the three and nine months ended September 30, 2003, respectively, and $7.9 million and $19.0 million for the corresponding periods in 2002.

The above transactions were recorded at fair value in accordance with our revenue recognition policy.

For the three and nine months ended September 30, 2003, one collaborator contributed 37% and 36% of total revenues, respectively. This includes a $4.4 million one-time fee related to this collaborator during the three months ended September 30, 2003. For the three months ended September 30, 2002, a different collaborator contributed 15% of total revenues. No single collaborator contributed 10% or more of revenues for the nine months ended September 30, 2002.

Two collaborators comprised 55% of the accounts receivable balance at September 30, 2003. Three collaborators comprised 45% of the accounts receivable balance at December 31, 2002.

8. Loss per share

For all periods presented, both basic and diluted net loss per common share are computed by dividing the net loss by the number of weighted average common shares during the period. Stock options and potential common shares issuable upon conversion of our subordinated notes were excluded from the computation of diluted net loss per share, as their share effect was antidilutive for all periods presented. The potential common shares that were excluded from the diluted net loss per share computation are as follows:

	September 30,	
	2003	2002
Outstanding stock options	8,695,555	9,176,797
Common shares issuable upon conversion of subordinated notes	2,469,667	2,525,956
Total potential common shares excluded from diluted net loss per share computation	11,165,222	11,702,753

9. Segment reporting

Our operations are treated as one operating segment, in accordance with FASB Statement No. 131 ("SFAS 131"). We recorded revenue from customers throughout the United States and in Austria, Belgium, Canada, Denmark, France, Germany, India, Israel, Japan, Sweden, Switzerland, and the United Kingdom. Export revenues for the three and nine months ended September 30, 2003 were $3.8 million and $10.9 million, respectively, and $6.9 million and $27.6 million for the three and nine months ended September 30, 2002, respectively.

10. Related party transactions

Incyte has entered into certain related party transactions as defined by FASB Statement No. 57, *Related Party Disclosures ("SFAS 57")*. In each of these transactions in which a director of Incyte is significantly affiliated with the other party to the transaction, such director has recused himself from voting on the related party transaction. Revenues from companies considered to be related parties as defined by SFAS 57 were $0.2 million and $0.2 million, for the three months ended September 30, 2003 and 2002, respectively, and $0.6 million and $1.4 million for the nine months ended September 30, 2003 and 2002, respectively. At September 30, 2003 and December 31, 2002, accounts receivable from related parties were $0.2 million and $0.6 million, respectively, and loans receivable from related parties were $0.2 million and $2.3 million, respectively. At September 30, 2003 and December 31, 2002, prepaid expenses to related parties were $0 million and $2.1 million, respectively.

11. Other expenses

Costs associated with restructuring activities initiated prior to December 31, 2002 are accounted for in accordance with EITF Issue No. 94-3 *Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring) ("EITF 94-3").* Accordingly, costs associated with such plans are recorded as other expenses in the consolidated statements of operations. Below is a summary of the activity related to other expenses recorded pursuant to EITF 94-3 for the periods in which activity related to our restructuring programs has taken place through the nine months ended September 30, 2003.

2002 Restructuring

(in thousands)	Nature of Charges	Original Charge Recorded in 2002	Accrual Balance as of December 31, 2002	2003 Charges to Operations	2003 Charges Utilized	Accrual Balance as of September 30, 2003
Restructuring expenses:						
Workforce reduction	Cash	$ 7,325	$ 4,867	$ —	$ (4,867)	$ —
Equipment and other assets	Non-cash	8,662	—	—	—	—
Lease commitments and other restructuring charges	Cash/Non-cash	17,924	18,504	262	(3,380)	15,386
Other expenses		$ 33,911	$ 23,371	$ 262	$ (8,247)	$ 15,386

During 2002, we recognized other expenses of $33.9 million relating to restructuring programs announced in the fourth quarter of 2002. During the nine months ended September 30, 2003, we recognized an additional charge of $0.3 million primarily relating to contract-related settlements and facilities lease expenses in excess of amounts originally estimated. We estimate that it may take us another nine months to sublease or otherwise terminate the leases for the various properties that have been vacated. We may incur additional costs associated with these subleasing and lease termination activities. We utilized $4.9 million of accrued severance charges and $3.4 million of accrued facilities and other restructuring charges during the nine months ended September 30, 2003. As of January 11, 2003, all affected employees had been terminated under this restructuring program.

The estimates above have been made based upon management's best estimate of the amounts and timing of certain events included in the restructuring plan that will occur in the future. It is possible that the actual outcome of certain events may differ from the estimates. Changes will be made to the restructuring accrual at the point that the differences become determinable.

2001 Restructuring and Other Impairments

(in thousands)	Nature of Charges	Original Charge Recorded in 2001	Accrual Balance as of December 31, 2002	2003 Charges to Operations	2003 Charges Utilized	Accrual Balance as of September 30, 2003
Restructuring expenses:						
Workforce reduction	Cash	$ 8,114	$ —	$ —	$ —	$ —
Equipment and other assets	Non-cash	32,629	—	—	—	—
Lease commitments and other restructuring charges	Cash/Non-cash	14,859	8,225	1,096	(8,683)	638
Subtotal		55,602	8,225	1,096	(8,683)	638
Impairment of goodwill and other intangible assets	Non-cash	68,666	—	—	—	—
Impairment of other long-lived assets	Non-cash	6,104	—	—	—	—
Other expenses		$ 130,372	$ 8,225	$ 1,096	$ (8,683)	$ 638

During 2001, we recognized other expenses of $130.4 million relating to restructuring programs and long-lived asset write-downs announced in the fourth quarter of 2001. During the nine months ended September 30, 2003, we recognized an additional charge of $1.1 million primarily relating to contract-related settlements and facilities lease expenses in excess of amounts originally estimated. We may incur additional costs associated with lease termination activities. We utilized $8.7 million of accrued facilities and other restructuring charges during the nine months ended September 30, 2003.

The estimates above have been made based upon management's best estimate of the amounts and timing of certain events included in the restructuring plan that will occur in the future. It is possible that the actual outcome of certain events may differ from the estimates. Changes will be made to the restructuring accrual at the point that the differences become determinable.

12. Purchased in-process research and development expenses

During 2003, we recorded $34.4 million of purchased in-process research and development expenses, consisting of $28.1 million for the acquisition of Maxia Pharmaceuticals, Inc. ("Maxia") and $6.3 million related to a collaborative license agreement with Pharmasset, Ltd. ("Pharmasset"). Below is a summary of the activity related to purchased in-process research and development expenses for the nine months ended September 30, 2003.

Acquisition of Maxia Pharmaceuticals, Inc.

In November 2002, we entered into an agreement to acquire Maxia, a privately-held company based in San Diego, California. On February 18, 2003, the acquisition was completed. Maxia was a drug discovery and development company that specialized in small molecule drugs targeting diabetes and other metabolic disorders, cancer, inflammatory diseases and heart disease. We acquired Maxia to create a more advanced and robust pipeline of discovery projects and product candidates and to further our drug discovery and development efforts.

The transaction was accounted for as an asset purchase pursuant to FASB 141, *Business Combinations*, as Maxia had not commenced its planned principal operations as described in EITF 98-3, *Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business*. The purchase price was preliminarily allocated as follows:

(in thousands)	
Net tangible liabilities assumed	$ (722.7)
In-process research and development	28,115.7
Total purchase price	$27,393.0

The total purchase price of approximately $27.4 million consists of approximately 4,476,092 shares of Incyte common stock with a fair value of $17.5 million, cash of approximately $5.6 million (consisting of $4.1 million cash paid to Maxia stockholders and a $1.5 million note payable from Maxia, issued in August 2002, that was applied to this transaction), direct transaction costs of $1.4 million and additional restructuring costs incurred as part of the acquisition of $2.9 million, in accordance with EITF Issue No. 95-3, *Recognition of Liabilities in Connection with a Purchase Business Combination ("EITF 95-3").* The value of the 4,476,092 shares of Incyte common stock was based on a per share price of $3.91. For valuation purposes, this per share price of Incyte common stock was determined as the average closing market price for the five trading days preceding February 18, 2003, the date on which the number of shares to be issued became determinable. As of September 30, 2003, 3,600,820 shares have been issued and $3.1 million have been paid to the former Maxia stockholders. Estimated direct transaction costs consist of fees for attorneys, accountants and filing costs. Of the total purchase price, up to 437,636 shares of our common stock and $500,000 in cash are payable to former Maxia stockholders on the second anniversary of the consummation of the merger and up to 437,636 shares of our common stock and $500,000 in cash are payable to former Maxia stockholders on the third anniversary of the consummation of the merger. We have paid these amounts and issued these shares into a third party escrow account.

The purchase price was allocated to the tangible assets acquired and liabilities assumed on the basis of their respective fair values on the acquisition date and to in-process research and development expense. Tangible assets acquired and liabilities assumed consist of cash of $0.5 million, prepaid expenses of $0.4 million, accounts payable of $0.8 million and accrued liabilities of $0.8 million. We recorded a charge at the time of acquisition for the purchase of in-process research and development expense ("IPRD") that is presented as a separate component of operating expenses; the valuation represents the estimated fair value of incomplete projects, that at the time of acquisition, had no alternative future use and for which technological feasibility had not been established. Incyte acquired three IPRD compounds that are in stages ranging from discovery to preclinical phases; management has determined that each of these projects would require significant further development before they would be available for release to customers. The preliminary allocations above are based on management's estimate of the purchase accounting at the date of acquisition and estimates will continue to be refined and the corresponding adjustments will be reflected in in-process research and development expenses. The purchase price allocation is subject to revision as management obtains additional information.

In accordance with EITF 95-3, we recorded a $2.9 million charge related to restructuring costs for Maxia, which consisted of workforce reductions and consolidation of facilities. We recorded employee termination costs of approximately $0.8 million for 28 employee positions. The job eliminations were completed in July 2003. We also recorded restructuring costs related to lease payments for property that has been vacated and other costs of $2.0 million. We estimate that it may take up to fifteen months to sublease or otherwise terminate the lease for the entire property in San Diego, California. During the nine months ended September 30, 2003, we have utilized $0.8 million of accrued severance charges and $0.6 million of accrued facilities and other restructuring costs.

We also recorded transaction costs related to the acquisition of $1.4 million and have utilized $0.9 million during the nine months ended September 30, 2003.

Below is a summary of activity related to accrued acquisition costs for the nine months ended September 30, 2003:

(in thousands)	Nature of Charge	Original Accrual	2003 Additions	2003 Accrual Utilized	Accrual Balance as of September 30, 2003
Accrued acquisition costs:					
Workforce reduction	Cash	$ 845	$ —	$ (845)	$ —
Lease commitments and other restructuring costs	Cash	2,016	—	(599)	1,417
Transaction fees	Cash	1,450	—	(887)	563
Accrued acquisition costs		$ 4,311	$ —	$ (2,331)	$ 1,980

The estimates above have been made based upon management's best estimate of the amounts and timing of certain events that will occur in the future. It is possible that the actual outcome of certain events may differ from the estimates. Changes will be made to this accrual at the point that the differences become determinable.

The condensed consolidated financial statements include the operating results of Maxia from February 18, 2003, the date of acquisition. Pro forma results of operations have not been presented because the effects of this acquisition were not material on either an individual or aggregate basis and the acquisition was accounted for as an acquisition of assets.

Under the merger agreement, former Maxia stockholders have the right to receive certain earn out amounts of up to a potential aggregate amount of $14.0 million upon the occurrence of certain milestones set forth in the merger agreement. Twenty percent of each earn out payment, if earned, will be paid in cash and the remaining eighty percent will be paid in shares of our common stock such that an aggregate of $2.8 million in cash and $11.2 million in our common stock could potentially be paid pursuant to the earn out milestones. The milestones occur as Maxia products enter various stages of human clinical trials and may be earned at any time prior to the tenth anniversary of the consummation of the merger. In any event, no more than 13,531,138 shares of our common stock may be issued to former Maxia stockholders in the aggregate pursuant to the merger agreement.

Collaborative License Agreement with Pharmasset, Ltd.

In September 2003, we entered into a collaborative licensing agreement with Pharmasset to develop and commercialize Reverset, an antiretroviral drug that is currently in Phase II clinical development for the treatment of HIV. Under the terms of the agreement we paid Pharmasset $6.3 million, which we recorded as a charge to purchased in-process research and development expense that is presented as a separate component of operating expenses. In addition to this payment, we also agreed to pay Pharmasset certain performance milestone payments and future royalties on net sales, in exchange for exclusive rights in the United States, Europe and certain other markets to develop, manufacture and market the drug. Pharmasset will retain marketing and commercialization rights in certain territories, including South America, Mexico, Africa, the Middle East and China.

13. Litigation

Invitrogen

On October 17, 2001, Invitrogen Corporation filed a complaint for patent infringement against Incyte in the United States District Court for the District of Delaware. On November 21, 2001, we filed our answer to Invitrogen's complaint. In addition, we asserted seven counterclaims against Invitrogen seeking declaratory relief with respect to the patents at issue, implied license, estoppel, laches, and patent misuse. We are also seeking our fees, costs, and expenses. Invitrogen filed its answer to our counterclaims on January 9, 2002. On February 25, 2003, we added a counterclaim for unfair business practices. On June 24, 2003, the Court stayed all proceedings pending final disposition of the appeal in a related case or entry of any order in any other action invalidating the same patents that are asserted in this case.

On November 21, 2001, we filed a complaint against Invitrogen, amended on December 21, 2001 and March 7, 2002, in the United States District Court for the Southern District of California alleging infringement of thirteen of its patents. Eight of the asserted patents are gene patents. Three of the patents relate to RNA amplification and gene expression. Two of the patents relate to methods of fabricating microarrays of biological samples. The complaint seeks a permanent injunction enjoining Invitrogen from further infringement of the patents at issue, damages for Invitrogen's conduct, as well as our fees, costs, and interest. We further seek triple damages based on Invitrogen's willful infringement of our patents. On April 2, 2002, Invitrogen filed its answer to our complaint and brought counterclaims against us seeking declaratory judgments that the patents in suit are invalid

and not infringed. Invitrogen also pled, but later withdrew, its affirmative defense and counterclaim alleging that one of our patents is unenforceable. On April 25, 2002, we filed our answer denying Invitrogen's counterclaims. Invitrogen has represented to the Court that its past sales of the eight GeneStorm cDNA clones charged with infringement of eight of our patents were not substantial and that it no longer sells these products. A stipulated two-month stay of all proceedings in this action was lifted on September 2, 2003. On October 2, 2003, this case was reassigned and the final pretrial conference in the case is scheduled for May 3, 2004.

We believe we have meritorious defenses and intend to defend the suit brought by Invitrogen vigorously. However, our defenses may be unsuccessful. At this time, we cannot reasonably estimate the possible range of any loss or damages resulting from these suits and counterclaims due to uncertainty regarding the ultimate outcome. In addition, regardless of the outcome, we expect that the Invitrogen litigation will result in future costs to us, which could be substantial. Further, there can be no assurance that any license that may be required as a result of this litigation will be available on commercially acceptable terms, if at all.

14. Subsequent event

We are currently in a dispute with a collaborator with respect to, among other things, payments that such collaborator alleges are owed to it under a contract between the parties. The collaborator alleges that we have repudiated our obligation to make future payments to the collaborator, in the aggregate amount of $28.25 million, through the remainder of the contract term ending in 2009. We believe that the collaborator's interpretation of the contract with respect to these payments is erroneous and that these payments are not owed. In addition, we have asserted issues of nonperformance on the part of the collaborator which we believe has failed to comply with certain of its contractual obligations to us.

On November 7, 2003, we received a letter from this collaborator informing us that it is initiating the arbitration process under the contract. If the disputed matter goes to final and binding arbitration, we intend to contest the collaborator's allegations and assert our issues vigorously. There can be no assurance as to the ultimate outcome of any such arbitration and at this time, we cannot predict the financial impact to us of the results of the arbitration.

PART I: FINANCIAL INFORMATION

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

This Management's Discussion and Analysis of Financial Condition and Results of Operations as of September 30, 2003 and for the three and nine month periods ended September 30, 2003 and 2002 should be read in conjunction with the unaudited condensed consolidated financial statements and notes thereto set forth in Item 1 of this report and the section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Company's Annual Report on Form 10-K for the year ended December 31, 2002.

When used in this discussion, the words "expects," "believes," "anticipates," "estimates," "may," "could," "intends," and similar expressions are intended to identify forward-looking statements. These statements, which include statements as to the impact of certain critical accounting policies on our financial results; expected expenses and expenditure levels; expected revenues and sources of revenues; expected uses of net cash; expected losses, net losses and net loss levels; expected expenditures including expenditures on intellectual property, research and development, new alliances and long term-investments; the offset of profits from certain products by other expenditures; the offset of continued expenditures on therapeutic discovery and development by expense reductions from the 2002 restructuring program; our plans to manage our information products to be cash flow positive; the adequacy of capital resources; the need to raise additional capital; the expected effect of our contractual obligations on our future liquidity and cash flow; our positions and the costs associated with resolving an arbitrated matter with a collaborator; our expectations regarding competition; our long-term investments, including anticipated expenditures, losses and expenses; the application of United States Patent and Trademark Office utility guidelines to our gene patent applications; costs associated with prosecuting, defending and enforcing patent claims and other intellectual property rights; the size of our intellectual property portfolio and its competitive position; our strategy with regard to protecting our intellectual property; the effect of pharmaceutical and biotechnology company consolidations, including reduced research and development spending and the softening of the market for genomic information and the market for our information products; the effect of our pharmaceutical and biotechnology customers' focus on late stage research and clinical products on the renewal of, pricing of, and the length of contractual commitment for our information products; the expected growth of, and our ability to manage expansion of, our therapeutic discovery and development operations; future required expertise relating to clinical trials, manufacturing, sales and marketing and for licenses to technology rights; the commercial availability of drugs resulting from our research; the time it may take to sublease or terminate the lease in San Diego, California; and our ability to obtain and maintain product liability and other insurance; are subject to risks and uncertainties that could cause actual results to differ materially from those projected. These risks and uncertainties include, but are not limited to, those risks discussed below, as well as the extent of utilization of genomic information by the biotechnology and pharmaceutical industries; actual and future consolidations of pharmaceutical and biotechnology companies; continuing trends with respect to reduced pharmaceutical and biotechnology research spending; our ability to manage our information products to be cash flow positive; risks relating to the development of new products and their use by our potential collaborators; the impact of technological advances and competition; unanticipated delays in research and development efforts; the result of further research; our ability to consolidate our facilities and to exit and close facilities upon anticipated timelines; our ability to deliver products and services to our customers effectively with reduced headcount and management and key employee diversion; our ability to obtain and retain customers; competition from other entities; early termination of a database collaboration agreement or failure to renew an agreement upon expiration; decreasing database revenues; the cost of accessing, licensing or acquiring technologies developed by other companies; significant delays or costs in obtaining regulatory approvals; failure to obtain regulatory approval; uncertainty as to the scope of coverage, enforceability or commercial protection from patents that issue on gene and other discoveries; our ability to obtain patent protection for our discoveries and to continue to be effective in expanding our patent coverage; the impact of changing laws on our patent portfolio; developments in and expenses relating to litigation and arbitration; the results of businesses in which we hold equity; and the matters discussed in "Factors That May Affect Results." These forward-looking statements speak only as of the date hereof. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

In the section of this report entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations—Factors That May Affect Results," all references to "Incyte," "we," "us," or "our" mean Incyte Corporation and our subsidiaries.

Incyte, LifeSeq, BioKnowledge and ZooSeq are our registered trademarks. We also refer to trademarks of other corporations and organizations in this document.

Overview

Incyte is a drug discovery company that develops proprietary genomic information and applies its expertise in medicinal chemistry and molecular, cellular and in vivo biology to the discovery of novel small molecule and protein therapeutics. Incyte believes it has created the largest commercial portfolio of issued United States patents covering human, full-length genes and the proteins they encode, and markets and licenses this information, as well as genomic and proteomic information, to many of the world's leading pharmaceutical and biotechnology companies and academic research centers. Incyte has assembled an experienced and talented drug discovery team that is identifying potential new drug therapies for cancer, inflammatory diseases and other medical conditions. Incyte has also in-licensed a compound for treatment of human immunodeficiency virus ("HIV") that is currently in clinical development.

We were incorporated in Delaware in April 1991 and, until 2001, devoted substantially all of our resources to the development, marketing and sales of genomics technologies and products to the biotechnology and pharmaceutical industries and research and academic institutions to aid in better and faster prevention, diagnosis and treatment of disease. Our products and services included databases, bioreagents, custom sequencing, gene expression, single nucleotide polymorphism, or SNP, discovery, and other services. Over time, we also increased our investments in growing our intellectual property estate to protect our proprietary information as well as our internal and collaborative efforts to identify and validate drug targets.

During 2001, we increased our focus on our therapeutic discovery and development programs, and we exited the following activities: microarray products and related services, genomic screening products and services, public domain clone products and related services, contract sequencing services, transgenic products and services and SNP discovery services.

Our business is now focused on our therapeutic discovery and development programs and our information products. Our current information products include databases, intellectual property licensing, funded research and cDNA clones. The fees and the period of access to our database information are negotiated independently with each customer. In addition to providing access to pharmaceutical and biotechnology customers, we also provide access to our database to third parties who use the database to develop genomic tools, such as microarrays that require genomic content, which they in turn sell to pharmaceutical and biotechnology researchers. Fees payable by pharmaceutical and biotechnology collaborators for our information products also generally consist of non-exclusive or exclusive fees corresponding to patent rights on proprietary genes and proteins. We may also receive future milestone and royalty payments from collaborators from the development and sale of their products derived from our technology and database information.

We expect that the overall market for our information products will continue to be competitive based on softening of the market for genomic information, shrinking research budgets of our current and potential customers and industry consolidation. Revenue trends indicate that subscribers are being more cautious with their spending to focus more of their resources on late stage research and clinical products than in the past, and this has adversely impacted renewals and the pricing of, and the length of the contractual commitment for, our information products. We expect this trend to continue at least through the remainder of 2003 and that revenues in 2003 will be lower than those recognized in the prior year.

We intend to manage our information products to be cash flow positive. Our ability to earn revenues and successfully manage our information products on a cash flow positive basis depends, in large part, on our ability to attract new customers and retain new and existing customers for our information products in an increasingly competitive market environment. Further, we have only received limited royalty revenues to date, and do not expect to receive significant royalty or other revenues from development and commercialization by our customers using our information products for several years, if at all. Revenues from our customers may be subject to significant fluctuation in both timing and amount and, therefore, our results of operations for any period may not be comparable to the results of operations for any other period.

In conjunction with the 2002 restructuring program, we have reduced certain expenses through a combination of decreased spending, job reductions and office consolidations and continued efforts to improve operational efficiencies. The restructuring program has had little impact on our therapeutic discovery and development programs as we intend to continue to invest in research and development for our therapeutic discovery and development efforts. We expect these expenses to continue to increase in 2003 and that these increases will partially offset our expense reductions from the 2002 restructuring program.

We anticipate incurring additional losses for the next several years as we expand our therapeutic drug discovery and development programs. We also expect that losses will fluctuate from quarter to quarter and that such fluctuations may be substantial. We do not expect to generate revenues from our therapeutic discovery and development efforts for several years, if at all. If we are unable to successfully develop and market pharmaceutical products over the next several years, our business, financial condition and results of operations would be adversely impacted.

Our long-term investments, as of September 30, 2003, consist of equity investments in privately-held companies; most of these investments were made in connection with the establishment of a collaborative arrangement between us and the investee company. Many of these companies are still in the start-up or development stage. Our investments in these companies are inherently risky because the technologies or products they have under development are typically in the early stages and may never become successful. The market values of many of these investments can fluctuate significantly. Current market conditions have caused us to write-down the value of our investments, resulting in charges to our earnings. The determination of investment impairment involves significant management judgment, and actual amounts realized for any specific investment may differ from recorded values. The market value of long-term investments that we hold can fluctuate significantly, and such fluctuations are highly variable and not within our control.

During 2002 and 2001, we reported charges of $37.3 million and $130.4 million, respectively, relating to restructuring programs and long-lived asset write-downs announced in the fourth quarter of each year. During the nine months ended September 30, 2003, we recorded an additional charge of $0.3 million and $1.1 million related to the 2002 and 2001 restructurings, respectively. A discussion of each of these restructuring programs follows.

During 2001, we exited certain product lines and, as a result of exiting these activities, we closed certain of our facilities in Fremont, California, Palo Alto, California, St. Louis, Missouri and Cambridge, United Kingdom. In addition to the product lines exited, we made infrastructure and other personnel reductions at our locations resulting in an aggregate workforce reduction of approximately 400 employees. A charge for the 2001 restructuring program and impairment of long-lived assets of $130.4 million was recorded in the fourth quarter of 2001 as a result of the change in focus. This charge was comprised of the following items: $68.7 million—goodwill and intangibles impairment; $55.6 million—restructuring charges (including $32.6 million in equipment and other assets impaired) and $6.1 million—impairment of a long-lived asset. Revenues from exited product lines for the years ended 2002 and 2001 were $3.6 million and $45.3 million, respectively. Additional charges for restructuring expenses of $3.4 million were recorded in 2002 and $1.1 million for the nine months ended September 30, 2003, primarily for contract-related settlements, impairment of long-lived assets and facilities lease expenses in excess of estimated amounts, offset by the release of other restructuring accruals in excess of actual expenses.

In November 2002, we announced plans to reduce our expenditures, primarily in research and development, through a combination of spending reductions, workforce reductions and office consolidations. The expense reduction plan included the elimination of approximately 37% of our workforce in Palo Alto, California, Beverly, Massachusetts, and Cambridge, England and consolidation of our office and research facilities in Palo Alto, California. As a result of these actions, we incurred a charge of $33.9 million during the fourth quarter of 2002. For the nine months ended September 30, 2003, we recorded an additional charge of $0.3 million relating to contract-related settlements and facilities lease expenses in excess of amounts originally estimated.

In November 2002, we entered into an agreement to acquire Maxia Pharmaceuticals, Inc. (“Maxia”), a privately-held company based in San Diego, California. On February 18, 2003, the acquisition was completed. Maxia was a drug discovery and development company that specialized in small molecule drugs targeting diabetes and other metabolic disorders, cancer, inflammatory diseases and heart disease. We acquired Maxia to create a more advanced and robust pipeline of discovery projects and product candidates and to further our drug discovery and development efforts.

The transaction was accounted for as an asset purchase pursuant to FASB 141, *Business Combinations*, as Maxia had not commenced its planned principal operations as described in EITF 98-3, *Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business*. The purchase price was preliminarily allocated as follows:

(in thousands)	
Net tangible liabilities assumed	$ (722.7)
In-process research and development	28,115.7
Total purchase price	$27,393.0

The total purchase price of approximately $27.4 million consists of approximately 4,476,092 shares of Incyte common stock with a fair value of $17.5 million, cash of approximately $5.6 million (consisting of $4.1 million cash paid to Maxia stockholders and a $1.5 million note payable from Maxia, issued in August 2002, that was applied to this transaction), direct transaction costs of $1.4 million and additional restructuring costs incurred as part of the acquisition of $2.9 million, in accordance with EITF Issue No. 95-3, *Recognition of Liabilities in Connection with a Purchase Business Combination (“EITF 95-3”).* The value of the 4,476,092 shares of Incyte common stock was based on a per share price of $3.91. For valuation purposes, this per share price of Incyte common stock was determined as the average closing market price for the five trading days preceding February 18, 2003, the date on which the number of shares to be issued became determinable. As of September 30, 2003, 3,600,820 shares have been issued and $3.1 million have been paid to the former Maxia stockholders. Estimated direct transaction costs consist of fees for attorneys, accountants and filing costs. Of the total purchase price, up to 437,636 shares of our common stock and $500,000 in cash are payable to former Maxia stockholders on the second anniversary of the consummation of the merger and up to 437,636

shares of our common stock and $500,000 in cash are payable to former Maxia stockholders on the third anniversary of the consummation of the merger. We have paid these amounts and issued these shares into a third party escrow account.

The purchase price was allocated to the tangible assets acquired and liabilities assumed on the basis of their respective fair values on the acquisition date and to in-process research and development expense. Tangible assets acquired and liabilities assumed consist of cash of $0.5 million, prepaid expenses of $0.4 million, accounts payable of $0.8 million and accrued liabilities of $0.8 million. We recorded a charge at the time of acquisition for the purchase of in-process research and development expense ("IPRD") that is presented as a separate component of operating expenses; the valuation represents the estimated fair value to incomplete projects, that at the time of acquisition, had no alternative future use and for which technological feasibility had not been established. Incyte acquired three IPRD compounds that are in stages ranging from discovery to preclinical phases; management has determined that each of these projects would require significant further development before they would be available for release to customers. The preliminary allocations above are based on management's estimate of the purchase accounting at the date of acquisition and estimates will continue to be refined and the corresponding adjustments will be reflected in in-process research and development expenses. The purchase price allocation is subject to revision as management obtains additional information.

In accordance with EITF 95-3, we recorded a $2.9 million charge related to restructuring costs for Maxia, which consisted of workforce reductions and consolidation of facilities. We recorded employee termination costs of approximately $0.8 million for 28 employee positions. The terminations were completed in July 2003. We also recorded restructuring costs related to lease payments for property that has been vacated and other costs of $2.0 million. We estimate that it may take up to fifteen months to sublease or otherwise terminate the lease for the entire property in San Diego, California. During the nine months ended September 30, 2003, we have utilized $0.8 million of accrued severance charges and $0.6 million of accrued facilities and other restructuring costs.

We also recorded transaction costs related to the acquisition of $1.4 million and have utilized $0.9 million during the nine months ended September 30, 2003.

Below is a summary of activity related to accrued acquisition costs for the nine months ended September 30, 2003:

(in thousands)	Nature of Charge	Original Accrual	2003 Additions	2003 Accrual Utilized	Balance as of September 30, 2003
Accrued acquisition costs:					
Workforce reduction	Cash	$ 845	$ —	$ (845)	$ —
Lease commitments and other restructuring costs	Cash	2,016	—	(599)	1,417
Transaction fees	Cash	1,450	—	(887)	563
Accrued acquisition costs		$ 4,311	$ —	$ (2,331)	$ 1,980

The estimates above have been made based upon management's best estimate of the amounts and timing of certain events that will occur in the future. It is possible that the actual outcome of certain events may differ from the estimates. Changes will be made to this accrual at the point that the differences become determinable.

The condensed consolidated financial statements include the operating results of Maxia from February 18, 2003, the date of acquisition. Pro forma results of operations have not been presented because the effects of this acquisition were not material on either an individual or aggregate basis and the acquisition was accounted for as an acquisition of assets.

Under the merger agreement, former Maxia stockholders have the right to receive certain earn out amounts of up to a potential aggregate amount of $14.0 million upon the occurrence of certain milestones set forth in the merger agreement. Twenty percent of each earn out payment, if earned, will be paid in cash and the remaining eighty percent will be paid in shares of our common stock such that an aggregate of $2.8 million in cash and $11.2 million in our common stock could potentially be paid pursuant to the earn out milestones. The milestones occur as Maxia products enter various stages of human clinical trials and may be earned at any time prior to the tenth anniversary of the consummation of the merger. In any event, no more than 13,531,138 shares of our common stock may be issued to former Maxia stockholders in the aggregate pursuant to the merger agreement.

In September 2003, we entered into a collaborative licensing agreement with Pharmasset, Ltd. ("Pharmasset") to develop and commercialize Reverset, an antiretroviral drug that is currently in Phase II clinical development for the treatment of HIV. Under the terms of the agreement we paid Pharmasset $6.3 million, which we recorded as a charge to purchased in-process research and development expense that is presented as a separate component of operating expenses. In addition to this payment, we also agreed to pay Pharmasset certain performance milestone payments and future royalties on net sales, in exchange for exclusive rights in the United States, Europe and certain other markets to develop, manufacture and market the drug. Pharmasset will retain

marketing and commercialization rights in certain territories, including South America, Mexico, Africa, the Middle East and China.

Critical Accounting Policies and Estimates

We believe the following critical accounting policies affect the more significant judgments and estimates used in the preparation of our condensed consolidated financial statements:

- Revenue recognition
- Valuation of long-lived assets
- Accounting for long-term investments
- Restructuring charges

Revenue Recognition. Revenues are recognized when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed and determinable and collectibility is reasonably assured. We enter into various types of agreements for access to our information databases, use of our intellectual property and sales of our custom products and services. Revenues are deferred for fees received before earned or until no further obligations exist.

Revenues from ongoing database agreements are recognized evenly over the access period. Revenues from licenses to our intellectual property are recognized when earned under the terms of the related agreements. Royalty revenues are recognized upon the sale of products or services to third parties by the licensee or other agreed upon terms. Revenues from custom products, such as clones and datasets, are recognized upon completion and delivery.

Revenues recognized from multiple element contracts are allocated to each element of the arrangement based on the fair values of the elements. The determination of fair value of each element is based on objective evidence from historical sales of the individual element by us to other customers. If such evidence of fair value for each undelivered element of the arrangement does not exist, all revenue from the arrangement is deferred until such time that evidence of fair value for each undelivered element does exist or until all elements of the arrangement are delivered. In accordance with Staff Accounting Bulletin No. 101, ("SAB 101"), when elements are specifically tied to a separate earnings process, revenue is recognized when the specific performance obligation associated with the element is completed. When revenues for an element are not specifically tied to a separate earnings process, they are recognized ratably over the term of the agreement.

When contracts include non-monetary payments, the value of the non-monetary transaction is determined using the fair value of the products and services involved, as applicable. For non-monetary payments involving the receipt of equity in a public entity, the fair value is based on the traded stock price on the date revenue is earned. For non-monetary payments involving the receipt of equity in a privately-held company, fair value is determined either based on a current or recent arm's length financing by the issuer or upon an independent valuation of the issuer.

In November 2002, the Emerging Issues Task Force ("EITF") of the Financial Accounting Standards Board issued EITF 00-21, *Revenue Arrangements with Multiple Deliverables*, which addresses certain aspects of the accounting for arrangements that involve the delivery or performance of multiple products, services and/or rights to use assets. Under EITF 00-21, revenue arrangements with multiple deliverables should be divided into separate units of accounting if the deliverables meet certain criteria, including whether the delivered items have stand alone value to the customer and whether there is objective and reliable evidence of the fair value of the undelivered items. In addition, the consideration should be allocated among the separate units of accounting based on their fair values, and the applicable revenue recognition criteria should be considered separately for each of the separate units of accounting. EITF 00-21 is effective for revenue arrangements we enter into after June 30, 2003. The application of EITF 00-21 did not have a material impact to our revenue arrangements for the three and nine month periods ended September 30, 2003.

Valuation of Long-Lived Assets. We assess the impairment of long-lived assets, which include property and equipment and intangible and other assets, whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors we consider important that could indicate the need for an impairment review include the following:

- Significant changes in the strategy of our overall business;
- Significant underperformance relative to expected historical or projected future operating results;
- Significant changes in the manner of use of the acquired assets;
- Significant negative industry or economic trends;

- Significant decline in our stock price for a sustained period; and
- Our market capitalization relative to net book value.

When we determine that the carrying value of long-lived assets may not be recoverable based upon the existence of one or more of the above indicators of impairment, in accordance with SFAS 144, we perform an undiscounted cash flow analysis to determine if impairment exists. If impairment exists, we measure the impairment based on the difference between the asset's carrying amount and its fair value.

Accounting for Long-Term Investments. We monitor our long-term investments for impairment on a periodic basis. As of September 30, 2003, our long-term investments consisted of equity investments in privately-held companies. Many of these companies are still in the start-up or development stage. Our investments in these companies are inherently risky because the technologies or products they have under development are typically in the early stages and may never become successful. Investments in publicly-traded companies are classified as available-for-sale and are adjusted to their fair value each period based on their traded market price with any adjustments being recorded in other comprehensive income. Investments in privately-held companies are carried at cost. We record an investment impairment charge when we believe that the investment has experienced a decline in value that is other than temporary. The determination of whether an impairment is other than temporary consists of a review of qualitative and quantitative factors by members of senior management. Generally, declines that persist for six months or more are considered other than temporary. We use the best information available in these assessments; however, the information available may be limited. These determinations involve significant management judgment, and actual amounts realized for any specific investment may differ from the recorded values. Future adverse changes in market conditions or poor operating results of underlying investments could result in additional impairment charges.

Restructuring Charges. The restructuring charges resulting from the 2002 and 2001 restructuring programs have been recorded in accordance with EITF Issue No. 94-3, *Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring) ("EITF 94-3")* and Staff Accounting Bulletin No. 100, *Restructuring and Impairment Charges ("SAB 100").* Any future restructuring activities initiated after December 31, 2002 will be recorded in accordance with FASB Statement No.146, *Accounting for Costs Associated with Exit or Disposal Activities ("SFAS 146").* Restructuring costs resulting from the Maxia acquisition have been recorded in accordance with EITF Issue No. 95-3, *Recognition of Liabilities in Connection with a Purchase Business Combination ("EITF 95-3").* The restructuring charges are comprised primarily of costs to exit facilities, reduce our workforce, write-off fixed assets, and costs of outside services incurred in the restructuring. The workforce reduction charge was determined based on the estimated severance and fringe benefit charge for identified employees. In calculating the cost to exit the facilities, we estimated the amount to be paid in lease termination payments for each location, the future lease and operating costs to be paid until the lease is terminated, the amount, if any, of sublease receipts and real estate broker fees. This required us to estimate the timing and costs of each lease to be terminated, the amount of operating costs, and the timing and rate at which we might be able to sublease the site. To form our estimates for these costs, we performed an assessment of the affected facilities and considered the current market conditions for each site. Estimates were also used in our calculation of the estimated realizable value on equipment that is being held for sale. These estimates were formed based on recent history of sales of similar equipment and market conditions. Our assumptions on either the lease termination payments, operating costs until terminated, the offsetting sublease receipts and estimated realizable value of fixed assets held for sale may turn out to be incorrect and our actual cost may be materially different from our estimates.

Results of Operations

We recorded a net loss of $43.0 million and $125.7 million and a basic and diluted net loss per share of $0.60 and $1.77 per share for the three and nine months ended September 30, 2003, respectively, as compared to $38.4 million and $69.4 million and $0.57 and $1.03 per share in the corresponding periods in 2002.

Revenues. Revenues for the three and nine months ended September 30, 2003 decreased to $13.2 million and $36.8 million, respectively, compared to $22.4 million and $80.5 million for the corresponding periods in 2002.

Information products, including database subscriptions, licensing of our intellectual property and partner programs, represented 100% of total net revenues for the three months and nine months ended September 30, 2003, respectively and 98% and 95% for the corresponding periods in 2002. During the three months ended September 30, 2003, total net revenue includes a $4.4 million one-time fee related to one collaborator. This one collaborator contributed 37% and 36% of total revenues for the three and nine months ended September 30, 2003, respectively. The decrease in revenues from 2002 reflects a softening in the market for genomic information, a reduction in research spending by pharmaceutical and biotechnology companies due in part to consolidations within these industries, their efforts to reduce spending and the accompanying impact on renewals and the price of, and length of contractual commitment for, our information products. Our database subscription and licensing revenues have been impacted as subscribers are being more cautious with their spending than in the past. Revenues for both the three and nine months ended September 30, 2003 included $0.0 million of revenue associated with the exited custom genomics product lines that was

announced in the fourth quarter of 2001 as compared to $0.5 million and $3.7 million for the three and nine months ended September 30, 2002.

Revenues received from agreements in which customers paid with equity securities in their company were $0 million for both the three and nine months ended September 30, 2003 and $0 million and $2.4 million for the three and nine months ended September 30, 2002. Additionally, revenues received from agreements in which we concurrently invested funds in the customer's stock were $0.2 million and $0.6 million for the three and nine months ended September 30, 2003, respectively, and $0.2 million and $0.6 million for the corresponding periods in 2002.

Revenues recognized from transactions in which there was originally a concurrent commitment entered into by us to purchase goods or services for the three and nine months ended September 30, 2003 were $0.8 million and $2.7 million, respectively. No transactions in which there was a concurrent commitment by us to purchase goods or services were entered into during the three and nine months ended September 30, 2003. Of commitments made in prior periods, we expensed $2.8 million and $8.3 million for the three and nine months ended September 30, 2003, respectively, and $7.9 million and $19.0 million for the corresponding periods in 2002.

The above transactions were recorded at fair value in accordance with our revenue recognition policy.

Operating Expenses. Total costs and expenses for the three and nine months ended September 30, 2003 were $43.4 million and $148.1 million, respectively, compared to $59.9 million and $159.6 million for the corresponding periods in 2002. In conjunction with the 2002 restructuring, we have reduced certain expenses through a combination of decreased spending, job reductions and office consolidations and continued efforts to improve operational efficiencies. The restructuring program has had little impact on our therapeutic discovery and development programs as we intend to continue to invest in research and development for our therapeutic discovery and development efforts. We expect these expenses to continue to increase through the remainder of 2003, and that such increases will partially offset our expense reductions from the 2002 restructuring program.

Research and development expenses. Research and development expenses for the three and nine months ended September 30, 2003 decreased to $28.6 million and $88.7 million, respectively, compared to $47.4 million and $118.8 million for the corresponding periods in 2002. The decrease in research and development expenses was primarily the result of expenses eliminated from the restructuring programs, partially offset by increased therapeutic discovery and development expenses.

Selling, general and administrative expenses. Selling, general and administrative expenses for the three and nine months ended September 30, 2003 decreased to $8.6 million and $23.7 million, respectively, compared to $12.1 million and $39.0 million for the corresponding periods in 2002. The decrease was primarily the result of expenses eliminated from the restructuring programs and decreased legal expenses, partially offset by general and administrative expenses incurred to support our therapeutic discovery and development efforts. Legal expenses related to our patent infringement lawsuits were approximately $0.8 million and $1.8 million in the three and nine months ended September 30, 2003, respectively, and $1.1 million and $4.1 million in the three and nine months ended September 30, 2002. Regardless of the outcome, our ongoing patent infringement litigation is expected to result in future costs to us, which could be substantial.

Purchased in-process research and development expense. Purchased in-process research and development expense for the three months ended September 30, 2003 of $6.3 million resulted from our collaborative licensing agreement with Pharmasset. Purchased in-process research and development expenses for the nine months ended September 30, 2003 of $34.4 million resulted from the acquisition of Maxia and our collaborative licensing agreement with Pharmasset.

Other expenses. Other expenses for the three and nine months ended September 30, 2003 of $0.0 million and $1.4 million, respectively, compared to $0.3 million and $1.7 million for the corresponding periods in 2002, represent charges recorded in connection with previously announced restructuring costs.

Interest and Other Income (Expense), Net. Interest and other income (expense), net, for the three and nine months ended September 30, 2003 decreased to $(11.3) million and $(7.5) million, respectively, from $1.6 million and $16.4 million for the corresponding period in 2002. The decrease for the three months ended September 30, 2003 was primarily due to $13.4 million of long-term investment impairment charges, a decrease in cash invested and lower interest rates in 2003, partially offset by a $0.8 million long-term investment gain in 2003. For the nine months ended September 30, 2003, the decrease was primarily due to $16.1 million of long-term investment impairment charges, a decrease in cash invested and lower interest rates in 2003, partially offset by a $0.8 million long term investment gain in 2003 and interest and premium earned on the conversion of a note held in another company in 2002.

Interest Expense. Interest expense for the three and nine months ended September 30, 2003 decreased to $2.3 million and $7.2 million, respectively, from $2.5 million and $7.4 million for the corresponding periods in 2002. The decrease was primarily due to the timing impact of the early retirement of $3.8 million face value of our convertible subordinated notes in 2003.

Gain on Repurchase of Convertible Subordinated Notes. Gain on repurchase of convertible subordinated notes for the three and nine months ended September 30, 2003 of $0.7 million was due to our repurchase of $3.8 million face value of our 5.5% convertible notes on the open market in the third quarter of 2003. Gain on repurchase of convertible subordinated notes for the nine months ended September 30, 2002 of $1.9 million was due to our repurchase of $6.7 million face value of these notes on the open market in the second quarter of 2002. In accordance with SFAS 145, all gains on the repurchase of convertible subordinated notes are presented as "Gain on repurchase of convertible subordinated notes".

Gain/(Loss) on Certain Derivative Financial Instruments, Net. Gain on certain derivative financial instruments for the three and nine months ended September 30, 2003 of $0.2 million and $0.3 million, respectively, and $0.2 million for the three months ended September 30, 2002 and loss on certain derivative financial instruments for the nine months ended September 30, 2002 of $0.3 million represent the change in the fair value of certain long-term investments, specifically warrants held in other companies, in accordance with FASB Statement No. 133 ("SFAS 133").

Provision for Income Taxes. Due to our net loss in 2003 and 2002, we had a minimal effective annual income tax rate. The income taxes for 2003 and 2002 are primarily attributable to foreign withholding taxes.

Liquidity and Capital Resources

As of September 30, 2003, we had $315.1 million in cash, cash equivalents and marketable securities, compared to $429.0 million as of December 31, 2002. We have classified all of our marketable securities as short-term, as we may choose not to hold them until maturity in order to take advantage of favorable market conditions. Available cash is invested in accordance with our investment policy's primary objectives of liquidity, safety of principal and diversity of investments.

Net cash used in operating activities was $98.4 million for the nine months ended September 30, 2003 as compared to $38.7 million for the nine months ended September 30, 2002. The increase was primarily due to the increase in net loss in 2003, adjusted for non-cash items such as purchased in-process research and development expense, depreciation and amortization, and impairment of long term investments, as well as higher cash usage for accrued and other current liabilities and a decrease in cash provided from accounts receivable.

Our investing activities, other than purchases, sales and maturities of marketable securities, have consisted predominantly of capital expenditures and net purchases of long-term investments. Capital expenditures for the nine months ended September 30, 2003 were $8.7 million as compared to $10.5 million in the same period in 2002. This decrease was primarily due to reduced operational needs related to our information products activities, partially offset by increased spending on our internal therapeutic discovery and development efforts. Purchases of long-term investments were $0 million and $5.0 million for the nine months ended September 30, 2003 and 2002, respectively. During the nine months ended September 30, 2003, we expended $5.1 million related to the acquisition of Maxia. In the future, net cash used by investing activities may fluctuate significantly from period to period due to the timing of long-term investments, acquisitions, including possible earn-out payments to former Maxia stockholders, capital expenditures and maturity/sales and purchases of marketable securities.

Net cash used in financing activities was $2.0 million for the nine months ended September 30, 2003 as compared to net cash provided of $1.3 million for the nine months ended September 30, 2002. We repurchased $3.8 million face value of our 5.5% convertible subordinated notes on the open market for $3.1 million in 2003, offset by proceeds from the issuance of common stock under our stock option and employee stock purchase plans of $1.2 million. In October 2002, we announced that our board of directors authorized the expenditure of up to $30.0 million to repurchase shares of our common stock in open market and privately negotiated transactions. Through September 30, 2003, we had purchased and retired 1,165,000 shares of common stock for an aggregate purchase price of $5.8 million. Net cash provided by financing activities for the nine months ended September 30, 2002 was primarily due to the repurchase of $6.7 million face value of our 5.5% convertible subordinated notes on the open market for $4.7 million, offset by proceeds from the issuance of common stock under our stock option and employee stock purchase plans of $5.9 million.

The following summarizes our future minimum long-term debt payments, future interest payments on long-term debt, and future operating lease payments for the next five fiscal years and thereafter as of September 30, 2003 and the effect those obligations are expected to have on our liquidity and cash flow in future periods (in millions):

	Total	Less Than 1 Year	Years 1–3	Years 4–5	Over 5 Years
Contractual Obligations:					
Principal on convertible subordinated debt	$ 166.5	$ —	$ —	$ 166.5	$ —
Interest on convertible subordinated debt	32.1	—	18.3	13.8	—
Non-cancelable operating lease obligations:					
Related to current operations	54.8	2.7	18.5	16.5	17.1
Related to vacated space	29.1	1.3	8.1	8.3	11.4
Total contractual obligations	$ 282.5	$ 4.0	$ 44.9	$ 205.1	$ 28.5

The amounts and timing of payments related to vacated facilities may vary based on timing of negotiation of lease terminations.

We have purchase commitments of $3.8 million at September 30, 2003, the timing of which is dependent upon provision by the vendor of products and services. Additionally, we have committed to purchase equity in a company when certain events occur. The total amount committed to purchase equity at September 30, 2003 was $5 million. These commitments are considered contingent commitments as future events must occur to cause the commitments to be enforceable.

Additional commitments related to Maxia and Pharmasset are also considered contingent commitments as future events must occur to cause these commitments to be enforceable. In February 2003, we completed our acquisition of Maxia. Under the merger agreement, former Maxia stockholders have the right to receive certain earn out amounts of up to a potential aggregate amount of $14.0 million upon the occurrence of certain milestones set forth in the merger agreement. Twenty percent of each earn out payment, if earned, will be paid in cash and the remaining eighty percent will be paid in shares of our common stock such that an aggregate of $2.8 million in cash and $11.2 million in our common stock could potentially be paid pursuant to the earn out milestones. The milestones occur as Maxia products enter various stages of human clinical trials and may be earned at any time prior to the tenth anniversary of the consummation of the merger. In any event, no more than 13,531,138 shares of our common stock may be issued to former Maxia stockholders in the aggregate pursuant to the merger agreement. None of these milestones has been achieved as of September 30, 2003.

In September 2003, we entered into a collaborative licensing agreement with Pharmasset to develop and commercialize Reverset, an antiretroviral drug that is currently in Phase II clinical development for the treatment of HIV. Under the terms of the agreement, we agreed to pay Pharmasset certain performance milestone payments and future royalties on net sales.

We expect to use net cash through the remainder of 2003 as we invest in our therapeutic discovery and development programs, including improvements to our laboratory facilities; continue to invest in our intellectual property portfolio; continue to seek access to technologies through investments, research and development and new alliances, license agreements and/or acquisitions; make payments related to our restructuring programs, including possible payments related to negotiated lease terminations; make long-term investments; repurchase our convertible subordinated notes or common stock and continue to make improvements in existing facilities.

We believe that our existing resources will be adequate to satisfy our capital needs for at least the next twelve months. Our cash requirements depend on numerous factors, including our ability to attract and retain collaborators for our databases and other products and services; expenditures in connection with alliances, license agreements and acquisitions of and investments in complementary technologies and businesses; expenditures in connection with our therapeutic discovery and development programs; competing technological and market developments; the cost of filing, prosecuting, defending and enforcing patent claims and other intellectual property rights; capital expenditures required for our therapeutic discovery and development programs; expenditures required to be made to terminate existing lease obligations; and costs associated with the integration of new operations assumed through mergers and acquisitions. Changes in our research and development or business plans or other changes affecting our operating expenses may result in changes in the timing and amount of expenditures of our capital resources.

FACTORS THAT MAY AFFECT RESULTS

RISKS RELATING TO OUR FINANCIAL RESULTS

We have had only limited periods of profitability, we expect to incur losses in the future and we may not return to profitability.

We had net losses from inception in 1991 through 1996 and in 1999 through the nine months ended September 30, 2003. Because of those losses, we had an accumulated deficit of $530.7 million as of September 30, 2003. We intend to continue to

spend significant amounts on new product and technology development, including the expansion of our research and development efforts for therapeutic discovery and development, the determination of the sequence of genes and the filing of patent applications regarding those gene sequences, the determination of gene functions, and our research and development alliances. As a result, we expect to incur losses in 2003. We expect to report net losses in future periods as well.

We expect that any cash flows from our information products, including our database products and our intellectual property licensing, will be more than offset by expenditures for our therapeutic discovery and development efforts. We anticipate that these efforts will increase as we focus on the studies that are required before we can sell, or license to a third party, a drug product. The development of therapeutic products will require significant expenses for research, development, testing and regulatory approvals. Unless we generate significant revenues to pay these costs, we will not return to profitability. We cannot be certain whether or when we will again become profitable because of the significant uncertainties relating to our ability to generate commercially successful drug products that will generate significant revenues.

Our operating results are difficult to predict, which may cause our stock price to decline and result in losses to investors.

Our operating results are difficult to predict and may fluctuate significantly from period to period, which may cause our stock price to decline and result in losses to investors. Some of the factors that could cause our operating results to fluctuate include:

- changes in the demand for our current and future products;
- the timing of intellectual property licenses that we may grant;
- the introduction of competitive databases or services, including databases of publicly available, or public domain, genetic information;
- the nature, pricing, length of commitments for and timing of products and services provided to our collaborators;
- our ability to compete effectively in our therapeutic discovery and development efforts against competitors that have greater financial or other resources or drug candidates that are in further stages of development;
- acquisition, licensing and other costs related to the expansion of our operations, including operating losses of acquired businesses;
- losses and expenses related to our investments;
- our ability to attract and retain key personnel;
- regulatory developments or changes in public perceptions relating to the use of genetic information and the diagnosis and treatment of disease based on genetic information;
- regulatory actions and changes related to the development of drugs;
- changes in intellectual property laws that affect our rights in genetic information that we license;
- payments of milestones, license fees or research payments under the terms of our external alliances and collaborations and our ability to monitor and enforce such payments;
- expenses related to, and the results of, litigation and other proceedings relating to intellectual property rights, including the lawsuits filed by Invitrogen and counterclaims filed by us, and
- risks and costs associated with our therapeutic discovery and development efforts and with advancing candidate compounds through clinical trials.

We anticipate significant fixed expenses, due in part to our expansion of our therapeutic discovery and development programs, and our continuing investment in product development and extensive support for our database collaborators. We may be unable to adjust our expenditures if revenues in a particular period fail to meet our expectations, which would harm our operating results for that period. Forecasting operating and integration expenses for acquired businesses may be particularly difficult, especially where the acquired business focuses on technologies that do not have an established market. We believe that period-to-period comparisons of our financial results will not necessarily be meaningful. You should not rely on these comparisons as an indication of our future performance. If our operating results in any future period fall below the expectations of securities analysts and investors, our stock price will likely decline, possibly by a significant amount. In addition, if market or

other economic conditions impact the stock market generally, or impact other companies in our industry, our stock price may also decline, possibly significantly.

If our long-term investments incur losses or charges, our earnings may decline or our losses may increase.

We make long-term investments in entities that complement our business. These investments may:

- often be made in securities lacking a public trading market or subject to trading restrictions, either of which increases our risk and reduces the liquidity of our investment;
- require us to record losses and expenses related to our ownership interest;
- require us to record charges related to the impairment in the value of the securities underlying our investment;
- require us to record acquisition-related charges, such as in-process research and development;
- require us to record charges related to post-acquisition impairment in the value of the acquired assets, such as goodwill or intangibles; and
- require us to invest greater amounts than anticipated or to devote substantial management time to the management of research and development or other relationships.

The market values of many of these investments can fluctuate significantly. We evaluate our long-term equity investments for impairment of their values on a quarterly basis. The volatility of the equity markets and the uncertainty of the biotechnology industry may result in fluctuations in the value of our investments in public companies. The value of our investments in private companies can fluctuate significantly. Current market conditions have caused us to write-down the value of our private company investments, and continuation of these conditions could cause us to write down additional amounts. Many private companies are encountering difficulties in raising capital in the current market, and even if they are successful, subsequent rounds of financing are often at lower valuations than previous rounds. Impairment could result in future charges to our earnings. Our strategic investments may cause our earnings to decline or our losses to increase.

Our debt investments are impacted by the financial viability of the underlying companies.

We have in the past and may in the future receive debt securities in the context of entering into a collaborative or other business relationship. The ability for these debt investments to be repaid upon maturity or to have a viable resale market is dependent, in part, on the financial success of the underlying company. Should the underlying company suffer significant financial difficulty, the debt instrument could either be downgraded or, in the worst case, our investment could be worthless. This would result in our losing the cash value of the investment and incurring a charge to our statement of operations.

Our database revenues could decline due to sequences becoming publicly available.

Our competitors may discover and establish patent positions with respect to the genes in our databases. Our competitors and other entities who engage in gene discovery may make the results of their sequencing efforts publicly available. Currently, academic institutions and other laboratories participating in the Human Genome Project make their gene sequence information available through a number of publicly available databases, including the GenBank database. The public availability of these discoveries or resulting patent positions covering substantial portions of the human genome could reduce the potential value of our databases to our collaborators. Public availability of sequences could also impair our ability to realize royalties or other revenue from any commercialized products based on genetic information made public prior to our patent filings.

Because our sales cycle is lengthy, we may spend a lot of time and money trying to obtain new or renewed subscriptions to our products but may be unsuccessful, which could hurt our profitability.

Our ability to obtain new customers for information products, to enter into license agreements for our intellectual property or to obtain renewals or additions to existing database product subscriptions, depends upon prospective subscribers' perceptions that our products and services can help accelerate their drug discovery efforts. Our database and licensing sales cycle is typically lengthy because we need to educate our potential subscribers and sell the benefits of our products to a variety of constituencies within potential subscriber companies. In addition, each agreement involves the negotiation of unique terms, and we may expend substantial funds and management effort with no assurance that a new, renewed or expanded agreement will result. These expenditures, without increased revenues, will negatively impact our profitability. Consolidations of pharmaceutical companies involved in drug discovery and development as well as expenditure reductions and an increased focus by our current or potential subscribers on later stage development programs and clinical compounds have affected the timing, progress and relative success of our sales and renewal efforts. We expect that any future consolidations and reductions in research budgets will have similar

effects. In addition, current or prospective subscribers may perceive us to be in competition with them given our therapeutic discovery and development efforts, which may adversely impact new sales or renewals.

We have a large amount of debt and our debt service obligations may prevent us from taking actions that we would otherwise consider to be in our best interests.

As of September 30, 2003, we had:

- total consolidated debt of $167.9 million,
- stockholders' equity of $194.1 million, and
- a deficiency of earnings available to cover fixed charges of $125.0 million for the nine months ended September 30, 2003.

A variety of uncertainties and contingencies will affect our future performance, many of which are beyond our control. We may not generate sufficient cash flow in the future to enable us to meet our anticipated fixed charges, including our debt service requirements with respect to our convertible subordinated notes due 2007 that we sold in February 2000. At September 30, 2003, $166.5 million face value of those notes were outstanding. The following table shows, as of September 30, 2003, the aggregate amount of our interest payments due in each of the next four calendar years listed:

Year	Aggregate Interest
2004	$ 9,157,775
2005	9,157,775
2006	9,157,775
2007	4,578,888

Our substantial leverage could have significant negative consequences for our future operations, including:

- increasing our vulnerability to general adverse economic and industry conditions;
- limiting our ability to obtain additional financing;
- requiring the dedication of a substantial portion of our expected cash flow to service our indebtedness, thereby reducing the amount of our expected cash flow available for other purposes, including working capital and capital expenditures;
- limiting our flexibility in planning for, or reacting to, changes in our business and the industry in which we compete; or
- placing us at a possible competitive disadvantage compared to less leveraged competitors and competitors that have better access to capital resources.

The capital markets may not permit us to raise additional capital at the time that we require it.

We believe that we have sufficient capital to satisfy our capital needs for at least the next twelve months. However, our future funding requirements will depend on many factors and we anticipate that, at some future point, we will need to raise additional capital to fund our business plan and research and development efforts on a going-forward basis. If we require additional capital at a time when investment in biotechnology companies such as ours, or in the marketplace generally, is limited due to the then prevailing market or other conditions, we may not be able to raise such funds at the time that we desire or any time thereafter.

Additional factors which may affect our future funding requirements include:

- any changes in the breadth of our research and development programs;
- the results of research and development, preclinical studies and clinical trials conducted by us or our future collaborative partners or licensees, if any;
- the acquisition or licensing of businesses, technologies or compounds, if any;

- our ability to maintain and establish new corporate relationships and research collaborations;
- competing technological and market developments;
- the amount of revenues generated from our business activities;
- the time and costs involved in filing, prosecuting, defending and enforcing patent and intellectual property claims;
- the receipt of contingent licensing or milestone fees from our current or future collaborative and license arrangements, if established; and
- the timing of regulatory approvals.

RISKS RELATING TO OUR BUSINESS AND INDUSTRY

Our workforce reduction and next-generation information product plans may have an adverse impact on our ability to deliver our information products on time, and we may fail to meet the expectations of our customers, which could in turn negatively impact our operating results.

In November 2002, we announced a reduction of approximately 37% of our workforce, including significant personnel reductions in our information product operations, in order to reduce expenses. Many factors, such as the reallocation of responsibilities among remaining personnel, the planned consolidation of our facilities and employee morale issues, may adversely impact our ability to deliver our products in accordance with our current plans or customer expectations, cause delays in the delivery of our products, or lead us to change our information product plans, which in turn may have a negative impact on our revenues and customer relationships. In addition, we announced plans in July 2003 to introduce the next-generation information product and to further streamline our information products operations. The implementation of the expense reduction program announced in November 2002 and the information product plans announced in July 2003 may result in customer concerns regarding our future performance and our ability to meet their expectations for our products, the diversion of efforts of our executive management team and other key employees, and higher than anticipated costs, any of which may negatively impact our operating results. Further, if our information products activities are not cash flow positive in future periods, further expense reductions may be necessary which, in turn, may also have a negative impact on our operating results.

In addition, we are relocating certain of our corporate functions to our facility in Wilmington, Delaware. Risks associated with this transition, including unanticipated delays, improper implementation or failure to retain certain key employees during crucial transition periods, could have a negative impact on our operating results.

Difficulties we may encounter managing the growth of our therapeutic discovery and development efforts may divert resources and limit our ability to successfully expand our business.

Our anticipated growth in the future of our therapeutic discovery and development programs, and our establishment of those operations places a strain on our infrastructure. As those operations expand, we expect that we will need to manage multiple locations and additional relationships with various collaborative partners, suppliers and other third parties. To manage our growth effectively, we must continue to improve our operational controls, reporting systems and procedures. We may not be able to successfully implement improvements to our systems and procedures in an efficient or timely manner.

Our industry is intensely competitive, and if we do not compete effectively, our revenues may decline and our losses may increase.

We compete in markets that are new, intensely competitive, rapidly changing, and fragmented. Many of our current and potential competitors have greater financial, human and other resources than we do. If we cannot respond quickly to changing customer requirements, secure intellectual property positions, or adapt quickly and obtain access to new and emerging technologies, our revenues may decline and commercial opportunities for any of our drug products may be reduced or eliminated. Our competitors include:

- Applera Corporation,
- Gene Logic Inc.,
- pharmaceutical and biotechnology companies, and
- universities and other research institutions.

The human genome contains a finite number of genes. Our competitors may seek to identify, sequence and determine the biological function of numerous genes in order to obtain a proprietary position with respect to new genes.

In addition, we face competition from companies who are developing and may seek to develop new technologies for discovering the functions of genes, gene expression information, including microarray technologies, discovery of variations among genes and related technologies. Also, if we are unable to obtain the technology we currently use or new advanced technology on acceptable terms, but other companies are, we will be unable to compete.

We also face competition from providers of software. A number of companies have announced their intent to develop and market software to assist pharmaceutical companies and academic researchers in managing and analyzing their own genomic data and publicly available data. If pharmaceutical companies and researchers are able to manage their own genomic data, or find software solutions for managing genomic data that they find preferable to those provided by us and our collaborators, they may not subscribe to our databases.

Extensive research efforts resulting in rapid technological progress characterize the genomics industry. To remain competitive, we must continue to expand our databases, improve our software, and invest in new technologies. New developments will probably continue, and discoveries by others, or the availability of such new discoveries in the public domain, may render our services and potential products noncompetitive.

We face significant competition for our therapeutic discovery and development efforts, and if we do not compete effectively, our commercial opportunity will be reduced or eliminated.

The biotechnology and pharmaceutical industries are intensely competitive and subject to rapid and significant technological change. Our therapeutic discovery and development efforts may target diseases and conditions that are already subject to existing therapies or that are subject to the drug discovery efforts of other entities. These competitors may develop products more rapidly or successfully than we or our collaborators are able to do. Our competitors might develop drugs that are more effective or less costly than any that are being developed by us or that would render our products obsolete and noncompetitive. In addition, our competitors may succeed in obtaining regulatory approvals for drug candidates more rapidly. Also, our competitors may obtain patent protection or other intellectual property rights that would limit our ability to develop competitive products. Any drugs resulting from our research and development efforts, or from our joint efforts with any future collaborators, might not be able to compete successfully with competitors' existing and future products or obtain regulatory approval in the United States or elsewhere.

We depend on key employees in a competitive market for skilled personnel, and the loss of the services of any of our key employees would affect our ability to achieve our objectives.

We are highly dependent on the principal members of our management, operations and scientific staff. Our product development, operations and marketing efforts could be delayed or curtailed if we lose the services of any of these people.

Our future success also will depend in part on the continued service of our executive management team, key scientific, bioinformatics and management personnel and our ability to train and retain essential scientific personnel for our therapeutic drug discovery and development programs. We experience intense competition for qualified personnel. If we are unable to continue to train and retain these personnel, we may be unable to execute our business plans successfully.

We rely on a small number of suppliers of certain products we need for our business and strategic collaborations with software providers for our information products, and if we are unable to obtain sufficient supplies, or maintain such strategic relationships, we will be unable to compete effectively.

We rely primarily on a strategic collaboration with one software provider to provide important functionality for our products. If this collaborator suffers business difficulties, or provides functionality that does not satisfy our customers' needs, or that our customers can find less expensively elsewhere, we may spend time and money to replace the functionality, we may not be able to deliver on customer commitments, and we may be otherwise adversely affected or our customer relationships and revenues may suffer.

If the information we obtain from third-party data sources is corrupt or violates the law, our revenues and operating results could decline.

We rely on and include in our databases scientific and other data supplied by others, including publicly available information from sources such as the Human Genome Project. This data could contain errors or other defects, which could corrupt our databases. In addition, we cannot guarantee that our data sources acquired this information in compliance with legal requirements. If this data caused database corruption or violated legal requirements, we would be unable to sell subscriptions to our databases. These lost sales would harm our revenue and operating results.

Security risks in electronic commerce, unfavorable Internet regulations, or business difficulties suffered by our collaborators may deter future use of our products, which could result in a loss of revenues.

We offer several products through our website on the Internet and may offer additional products in the future. Our ability to provide secure transmissions of confidential information over the Internet may limit online use of our products and services by our database collaborators as we may be limited by our inability to provide secure transmissions of confidential information over the Internet. Advances in computer capabilities and new discoveries in the field of cryptography may compromise the security measures we use to protect our website, access to our databases, and transmissions to and from our website. If our security measures are breached, our proprietary information or confidential information about our collaborators could be misappropriated. Also, a security breach could result in interruptions in our operations. The security measures we adopt may not be sufficient to prevent breaches, and we may be required to incur significant costs to protect against security breaches or to alleviate problems caused by breaches. Further, if the security of our website, or the website of another company, is breached, our collaborators may no longer use the Internet when the transmission of confidential information is involved. For example, recent attacks by computer hackers on major e-commerce websites and other Internet service providers have heightened concerns regarding the security and reliability of the Internet.

Because of the growth in electronic commerce, the United States Congress has held hearings on whether to further regulate providers of services and transactions in the electronic commerce market. The federal government could enact laws, rules and regulations that would affect our business and operations. Individual states could also enact laws regulating the use of the Internet. If enacted, these federal and state laws, rules and regulations could require us to change our online business and operations, which could limit our growth and our development of our online products.

Because our revenues are derived primarily from the pharmaceutical and biotechnology industries, our revenues may fluctuate substantially due to reductions and delays in research and development expenditures.

We expect that our revenues in the foreseeable future will be derived primarily from products and services provided to the pharmaceutical and biotechnology industries as well as to the academic community. Accordingly, our success will depend in large part upon the success of the companies within these industries and their demand for our products and services. Our operating results may fluctuate substantially due to reductions and delays in research and development expenditures by companies in these industries or by the academic community. These reductions and delays may result from factors such as:

- changes in economic conditions;
- consolidation in the pharmaceutical and biotechnology industries;
- changes in the regulatory environment, including governmental pricing controls, affecting health care and health care providers;
- pricing pressures;
- market-driven pressures on companies to consolidate and reduce costs; and
- other factors affecting research and development spending.

These factors are not within our control.

We are at the early stage of our therapeutic discovery and development efforts and we may be unsuccessful in our efforts.

We are in the early stage of building our therapeutic discovery and development operations. Our ability to develop and commercialize pharmaceutical products based on proteins, antibodies and other compounds will depend on our ability to:

- hire and retain key scientific employees;
- identify high quality therapeutic targets;
- identify potential therapeutic candidates;
- develop products internally;
- complete laboratory testing and human studies;

- obtain and maintain necessary intellectual property rights to our products;
- obtain and maintain necessary regulatory approvals related to the efficiency and safety of our products;
- enter into arrangements with third parties to provide services or manufacture our products on our behalf or develop efficient production facilities meeting all regulatory requirements;
- deploy sales and marketing resources effectively or enter into arrangements with third parties to provide these functions;
- lease facilities at reasonable rates to support our growth; and
- enter into arrangements with third parties to license and commercialize our products.

We have limited corporate experience with these activities and may not be successful in developing or commercializing drug products. If we choose to outsource some of these activities, we may be unable to enter into outsourcing or licensing agreements on commercially reasonable terms, or at all. In addition, if we, in the future, elect to manufacture our products in our own manufacturing facilities, those facilities will require substantial additional capital resources, and we will need to attract and retain qualified personnel to build or lease or operate any such facilities.

The success of our therapeutic discovery and development efforts may depend on our ability to find collaborators or other service providers to leverage our capabilities, and if we are unable to establish future collaborations or if these future collaborations are unsuccessful, our research and development efforts could be negatively affected.

Our strategy may depend in part upon the formation and sustainability of multiple collaborative arrangements and license agreements with third parties in the future. We may rely on these arrangements for not only financial resources, but also for expertise or economies of scale that we expect to need in the future relating to clinical trials, manufacturing, sales and marketing, and for licenses to technology rights. In order for any future collaboration efforts to be successful, we must first identify potential collaborators whose capabilities complement and integrate well with ours. Our collaborators may prove difficult to work with or less skilled than we originally expected.

It is likely that we will not be able to control the amount and timing of resources that our future corporate collaborators devote to our programs or potential products. We do not know whether our future collaborators, if any, might pursue alternative technologies or develop alternative products either on their own or in collaboration with others, including our competitors, as a means for developing treatments for the diseases targeted by collaborative arrangements with us. Conflicts also might arise with future collaborative partners concerning proprietary rights to particular compounds.

We might not be able to commercialize our therapeutic product candidates successfully, and we may spend significant time and money attempting to do so.

At the present time, we have only begun to identify potential therapeutic compounds from our internal programs and have yet to put them into clinical testing. Of the compounds we identify as potential therapeutic candidates, at most, only a few are statistically likely to lead to successful therapeutic development efforts. We expect drugs that result from our research will not be commercially available for a number of years, if at all. Commercialization of any product candidates that we identify and develop, or that we license from collaborators such as Pharmasset and develop, depends on successful completion of preclinical studies and clinical trials. Preclinical testing and clinical development are long, expensive and uncertain processes, and we do not know whether we, or any of our future collaborators, will be permitted to undertake clinical trials of any potential products. It may take us or any of our future collaborators several years to complete any such testing, and failure can occur at any stage of testing. Interim results of trial do not necessarily predict final results, and acceptable results in early trials may not be repeated in later trials. Data obtained from tests are susceptible to varying interpretation, which may delay, limit or prevent regulatory approval. Regulatory authorities may refuse or delay approval as a result of many other factors, including changes in regulatory policy during the period of product development. A number of companies in the pharmaceutical industry, including biotechnology companies, have suffered significant setbacks in advanced clinical trials, even after achieving promising results in earlier trials. Moreover, if and when our products reach clinical trials, we, or our future collaborators, may decide to discontinue development of any or all of these products at any time for commercial, scientific or other reasons. There is also a risk that competitors and third parties may develop similar or superior products or have proprietary rights that preclude us from ultimately marketing our products, as well as the potential risk that our products may not be accepted by the marketplace.

Completion of clinical trials may take many years. The length of time required varies substantially according to the type, complexity, novelty and intended use of the product candidate. Our rate of commencement and completion of clinical trials may be delayed by many factors, including:

- our inability to manufacture sufficient quantities of materials for use in clinical trials;

- variability in the number and types of patients available for each study;
- difficulty in maintaining contact with patients after treatment, resulting in incomplete data;
- unforeseen safety issues or side effects;
- poor or unanticipated effectiveness of products during the clinical trials; or
- government or regulatory delays.

An important element of our business strategy will be to enter into collaborative arrangements with third parties under which we license our therapeutic product candidates to those third parties for development and commercialization. We face significant competition in seeking appropriate collaborators. Also, these arrangements are complex to negotiate and time-consuming to document. We may not be successful in our attempts to establish these arrangements. The terms of any such arrangements that we establish may not be favorable to us. Further, any such arrangements may be unsuccessful.

We may encounter difficulties in integrating companies we acquire, and our operations and financial results could be harmed.

As part of our business strategy we acquire assets, technologies, compounds and businesses. Our past acquisitions, including our recent acquisition of Maxia Pharmaceuticals, Inc., have involved, and our future acquisitions may involve risks such as the following:

- we may be exposed to unknown liabilities of acquired companies;
- our acquisition and integration costs may be higher than we anticipated and may cause our quarterly and annual operating results to fluctuate;
- we may experience difficulty and expense in assimilating the operations and personnel of the acquired businesses, disrupting our business and diverting management's time and attention;
- we may be unable to integrate or complete the development and application of acquired technology, or compounds;
- we may experience difficulties in establishing and maintaining uniform standards, controls, procedures and policies;
- our relationships with key customers of acquired businesses may be impaired, due to changes in management and ownership of the acquired businesses;
- we may be unable to retain key employees of the acquired businesses;
- we may incur amortization or impairment expenses if an acquisition results in significant goodwill or other intangible assets; or
- our stockholders may be diluted if we pay for the acquisition with equity securities.

In addition, if we acquire additional businesses that are not located near existing sites, we may experience more difficulty integrating and managing the acquired businesses' operations.

If product liability lawsuits are successfully brought against us, we could face substantial liabilities and may be required to limit commercialization of our products.

The testing and marketing of medical products entails an inherent risk of product liability. If we cannot successfully defend ourselves against product liability claims, we may incur substantial liabilities or be required to limit commercialization of our products. Although we intend to obtain product liability insurance, this insurance may be prohibitively expensive, or may not fully cover our potential liabilities. Our inability to obtain sufficient product liability insurance at an acceptable cost to protect against potential product liability claims could prevent or inhibit the commercialization of pharmaceutical products we develop, alone or with our future collaborators. We, or our future collaborators, might not be able to obtain insurance at a reasonable cost, if at all.

We conduct our drug discovery and development operations at a single site.

Our research and development activities are conducted solely at our facility in Wilmington, Delaware. Our lease contains provisions that provide for its early termination upon the occurrence of certain events of default or upon a change of control. If we were to lose access to our Wilmington, Delaware, facility, either on a temporary or permanent basis, or if our lease to this facility were to terminate prior to the expiration of its full term, this could result in an interruption of our business and, consequently, could adversely impact the advancement of our drug discovery and development programs and our business.

If a natural disaster occurs, we may have to cease or limit our business operations.

We conduct our information products activities and a significant portion of our administrative functions at our facility in Palo Alto, California, which is in a seismically active area. Although we maintain business interruption insurance, we do not have and do not plan to obtain earthquake insurance. A major catastrophe, such as an earthquake or other natural disaster, could result in a prolonged interruption of our business.

RISKS RELATING TO CUSTOMERS AND COLLABORATORS

To generate significant revenues, we must obtain additional database customers and retain existing customers.

Our revenues are dependent on our ability to attract new customers and to retain existing customers. If we are unable to enter into additional agreements, or if our current database customers choose not to renew their agreements upon expiration or choose to renew their agreements at lower prices or for shorter durations, we may not generate additional revenues or maintain our current revenues. Our database revenues are also affected by the extent to which existing customers expand their agreements to include our new database products, the extent to which existing customers reduce the number of products for which they subscribe, and the number of product offerings that we offer, the impact of which will vary based upon our pricing of, or eliminations of, those products, as well as the pricing of new information product offerings. If the market for genomic information continues to soften, we may be required to lower prices further or restructure our product offerings to continue to meet customer demands which, in turn, may adversely impact our revenues. Some of our database agreements require us to meet performance obligations, some or all of which we may not be successful in attaining. A database customer can terminate its agreement before the end of its scheduled term if we breach the agreement and fail to cure the breach within a specified period. In addition, it is likely that database revenues will decrease if we are successful in entering into co-development arrangements with some of our current database subscribers to develop new therapeutic products.

Licensing our gene-related intellectual property may not contribute significantly to revenues for several years, and may never result in revenues.

Part of our strategy is to license to database customers and to some of our other customers our know-how and patent rights associated with the genetic information in our proprietary databases, for use in the discovery and development of potential pharmaceutical, diagnostic or other products. Any potential product that is the subject of such a license will require several years of further development, clinical testing and regulatory approval before commercialization. Therefore, milestone or royalty payments from these collaborations may not contribute to revenues for several years, if at all.

If conflicts arise between our future collaborators or advisors and us, they may act in their self-interest, which may be adverse to our interests or to the interests of our stockholders.

If conflicts arise between us and our future corporate collaborators or future scientific advisors, the other party may act in its self-interest and not in the interest of our stockholders. It is likely that many of our future collaborators will be conducting multiple product development efforts within each disease area that is the subject of the collaboration with us. Our future corporate collaborators may develop, either alone or with others, products in related fields that are competitive with the products or potential products that are the subject of these collaborations. Competing products, either developed by our future collaborators or to which our future collaborators have rights, may result in their withdrawal of support for our product candidates.

If we fail to enter into future in-licensing or collaborative arrangements or if these arrangements are unsuccessful, our business and operations would be negatively impacted.

We do not know if we will be able to establish collaborative arrangements, or whether any such future in-licensing or collaborative arrangements will ultimately be successful. For example, there have been, and may continue to be, a significant number of recent business combinations among large pharmaceutical companies that have resulted, and may continue to result, in a reduced number of potential future corporate collaborators. This consolidation may limit our ability to find partners who will work with us in developing and commercializing drugs. If business combinations involving our existing corporate collaborators were to occur, the effect could be to diminish, terminate or cause delays in one or more of our corporate collaborations or agreements. If we are unable to enter into collaborative arrangements or if those arrangements are unsuccessful, our research and

development efforts could be negatively impacted and we may need to seek additional capital resources during times when those resources may not be available or are available on less favorable terms.

RISKS RELATING TO INTELLECTUAL PROPERTY

We are involved in patent litigation, which if not resolved favorably, could require us to pay damages.

We are currently involved in patent litigation.

In October 2001, Invitrogen Corporation filed an action against us in federal court, alleging infringement of three patents that relate to the use of reverse transcriptase with no RNase H activity in preparing complimentary DNA from RNA. The complaint seeks unspecified money damages and injunctive relief. In November 2001, we filed our answers to Invitrogen's patent infringement claims, and asserted seven counterclaims against Invitrogen, seeking declaratory relief with respect to the patents at issue, implied license, estoppel, laches, and patent misuse. We are also seeking our fees, costs and expenses. Invitrogen filed its answer to our counterclaims in January 2002. In February 2003, we added a counterclaim for unfair business practices. In June 2003, the Court stayed all proceedings pending final disposition of the appeal in a related case or entry of any order in any other action invalidating the same patents that are asserted in this case. In November 2001, we filed a complaint against Invitrogen in federal court alleging infringement of 13 of our patents relating to genes, RNA amplification and gene expression, and methods of fabricating microarrays of biological samples. The complaint seeks a permanent injunction enjoining Invitrogen from further infringement of the patents at issue, damages for Invitrogen's conduct, as well as our fees, costs, and interest. We are further seeking triple damages from the infringement claim based on Invitrogen's willful infringement of our patents. In April 2002, Invitrogen filed answers to our patent infringement claims and brought counterclaims against us seeking declaratory judgments that the patents in suit are invalid and not infringed. Invitrogen also pled, but later withdrew, its affirmative defense and counterclaim alleging one of our patents is unenforceable. In April 2002, we filed our answer denying Invitrogen's counterclaims. Invitrogen has represented to the Court that its past sales of the eight of our gene patents were not substantial and that it no longer sells these products. On July 2, 2003, the Court entered a stipulated two-month stay of all proceedings in this action. A stipulated two-month stay of all proceedings in this action was lifted on September 2, 2003. On October 2, 2003, this case was reassigned and the final pretrial conference in the case is scheduled for May 3, 2004.

We believe we have meritorious defenses and intend to defend the suit brought by Invitrogen vigorously. However, our defenses may be unsuccessful. At this time, we cannot reasonably estimate the possible range of any loss or damages resulting from these suits and counterclaims due to uncertainty regarding the ultimate outcome. In addition, regardless of the outcome, we expect that the Invitrogen litigation will result in future costs to us, which could be substantial. Further, there can be no assurance that any license that may be required as a result of this litigation will be available on commercially acceptable terms, if at all.

If we are subject to additional litigation and infringement claims, they could be costly and disrupt our business.

The technology that we use to develop our products, and the technology that we incorporate in our products, may be subject to claims that they infringe the patents or proprietary rights of others. The risk of this occurring will tend to increase as the genomics, biotechnology and software industries expand, more patents are issued and other companies attempt to discover genes and SNPs and engage in other genomic-related businesses. The success of our therapeutic discovery and development efforts will also depend, in part, on our ability to operate without infringing or misappropriating the proprietary rights of others.

As is typical in the genomics, biotechnology and software industries, we have received, and we will probably receive in the future, notices from third parties alleging patent infringement. Except for Invitrogen, no third party has a current filed patent lawsuit against us.

We may, however, be involved in future lawsuits alleging patent infringement or other intellectual property rights violations. In addition, litigation may be necessary to:

- assert claims of infringement;
- enforce our patents;
- protect our trade secrets or know-how; or
- determine the enforceability, scope and validity of the proprietary rights of others.

We may be unsuccessful in defending or pursuing these lawsuits. Regardless of the outcome, litigation can be very costly and can divert management's efforts. An adverse determination may subject us to significant liabilities or require us or our future collaborators to seek licenses to other parties' patents or proprietary rights. We or our future collaborators may also be restricted

or prevented from manufacturing or selling our products and services. Further, we or our future collaborators may not be able to obtain any necessary licenses on acceptable terms, if at all.

We may be unable to protect our proprietary information, which may result in its unauthorized use and a loss of revenue.

Our business and competitive position depend upon our ability to protect our proprietary database information and software technology. Despite our efforts to protect this information and technology, unauthorized parties may attempt to obtain and use information that we regard as proprietary. Although our database subscription agreements require our subscribers to control access to our databases, policing unauthorized use of our databases and software may be difficult, both domestically and internationally.

We pursue a policy of having our employees, consultants and advisors execute proprietary information and invention agreements when they begin working for us. However, these agreements may not provide meaningful protection for our trade secrets or other proprietary information in the event of unauthorized use or disclosure.

Our means of protecting our proprietary rights may not be adequate, and our competitors may:

- independently develop substantially equivalent proprietary information and techniques;
- otherwise gain access to our proprietary information; or
- design around patents issued to us or our other intellectual property.

If the inventions described in our patent applications on full-length or partial genes, proteins and antibodies are found to be unpatentable, our issued patents are not enforced or our patent applications conflict with patent applications filed by others, our revenues may decline.

One of our strategies is to file patent applications on what we believe to be novel full-length and partial genes, proteins, antibodies and SNPs obtained through our efforts to discover the order, or sequence, of the molecules, or bases, of genes. We have filed U.S. patent applications in which we claimed partial genes. We have also applied for patents in the U.S. and other countries claiming full-length genes associated with cells and tissues involved in our gene sequencing program. We hold a number of issued U.S. patents on full-length genes, the proteins they encode and antibodies directed against them and one issued U.S. patent claiming multiple partial genes. While the United States Patent and Trademark Office has issued patents covering full-length genes, partial genes and SNPs, the Patent and Trademark Office may choose to interpret new guidelines for the issuance of patents in a more restrictive manner in the future, which could affect the issuance of our pending patent applications. We also do not know whether or how courts may enforce our issued patents, if that becomes necessary. If a court finds these types of inventions to be unpatentable, or interprets them narrowly, the value of our patent portfolio and possibly our revenues could be diminished.

We believe that some of our patent applications claim genes and partial genes that may also be claimed in patent applications filed by others. In some or all of these applications, a determination of priority of inventorship may need to be decided in an interference before the United States Patent and Trademark Office, before a patent is issued. If a full-length or partial length genes for which we seek a patent is issued to one of our competitors, we may be unable to include that full-length or partial length gene in a library of bioreagents. This could result in a loss of revenues.

If the effective term of our patents is decreased due to changes in the United States patent laws or if we need to refile some of our patent applications, the value of our patent portfolio and the revenues we derive from it may be decreased.

The value of our patents depends in part on their duration. A shorter period of patent protection could lessen the value of our rights under any patents that we obtain and may decrease the revenues we derive from our patents. The U.S. patent laws were amended in 1995 to change the term of patent protection from 17 years from patent issuance to 20 years from the earliest effective filing date of the application. Because the average time from filing to issuance of biotechnology applications is at least one year and may be more than three years depending on the subject matter, a 20-year patent term from the filing date may result in substantially shorter patent protection. Also, we may need to refile some of our applications claiming large numbers of genes and, in these situations, the patent term will be measured from the date of the earliest priority application. This would shorten our period of patent exclusivity and may decrease the revenues that we might obtain from the patents.

If patent application filing fees are significantly increased, our expenses related to intellectual property or our intellectual property strategy may be adversely affected.

Our ability to license proprietary genes may be dependent on our ability to obtain patents. We believe we have the largest commercial portfolio of issued U.S. patents covering human full-length genes, the proteins they encode and the antibodies directed against them. If legislation currently proposed by the United States Patent and Trademark Office is adopted, fees associated with filing and prosecuting patent applications would increase significantly. If such fees are significantly increased, we would incur higher expenses and our intellectual property strategy could be adversely affected.

International patent protection is particularly uncertain, and if we are involved in opposition proceedings in foreign countries, we may have to expend substantial sums and management resources.

Biotechnology patent law outside the U.S. is even more uncertain than in the U.S. and is currently undergoing review and revision in many countries. Further, the laws of some foreign countries may not protect our intellectual property rights to the same extent as United States laws. We may participate in opposition proceedings to determine the validity of our foreign patents or our competitors' foreign patents, which could result in substantial costs and diversion of our efforts.

REGULATORY RISKS

If we are unable to obtain regulatory approval to develop and market products in the United States and foreign jurisdictions, we or our future collaborators might not be permitted to commercialize products from our research.

Before commencing clinical trials in humans, we, or our future collaborators, will need to submit and receive approval from the FDA of an Investigational New Drug application, or IND. The regulatory process also requires preclinical testing. Data obtained from preclinical and clinical activities are susceptible to varying interpretations, which could delay, limit or prevent regulatory approval. In addition, delays or rejections may be encountered based upon changes in regulatory policy for product approval during the period of product development and regulatory agency review. Any failure to obtain regulatory approval could delay or prevent us from commercializing products.

Due, in part, to the early stage of our drug candidate research and development process, we cannot predict whether regulatory approval will be obtained for any product we, or our future collaborators, hope to develop. Significant research and development efforts will be necessary before any products can be commercialized. Satisfaction of regulatory requirements typically takes many years, is dependent upon the type, complexity and novelty of the product and requires the expenditure of substantial resources.

If regulatory approval of a product is granted, this approval will be limited to those disease states and conditions for which the product is demonstrated through clinical trials to be safe and efficacious. We cannot ensure that any compound developed by us, alone or with others, will prove to be safe and efficacious in clinical trials and will meet all of the applicable regulatory requirements needed to receive marketing approval.

Outside the United States, our ability, or that of our future collaborative partners, to market a product is contingent upon receiving a marketing authorization from the appropriate regulatory authorities. This foreign regulatory approval process typically includes all of the risks associated with FDA approval described above and may also include additional risks.

Because our activities involve the use of hazardous materials, we may be subject to claims relating to improper handling, storage or disposal of these materials that could be time consuming and costly.

Our research and development processes involve the controlled use of hazardous and radioactive materials and biological waste. Our operations produce hazardous waste products. We cannot eliminate the risk of accidental contamination or discharge and any resultant injury from these materials. We are subject to federal, state and local laws and regulations governing the use, manufacture, storage, handling and disposal of these materials and waste products. We may be sued for any injury or contamination that results from our use or the use by third parties of these materials, and our liability may exceed our insurance coverage and our total assets. Compliance with environmental laws and regulations may be expensive, and current or future environmental regulations may impair our research, development and production efforts.

Future changes to environmental, health and safety laws could cause us to incur additional expense or restrict our operations. In addition, our future collaborators may use hazardous materials in connection with our collaborative efforts. To our knowledge, their work is performed in accordance with applicable biosafety regulations. In the event of a lawsuit or investigation, however, we could be held responsible for any injury caused to persons or property by exposure to, or release of, these hazardous materials used by these parties. Further, we may be required to indemnify our collaborators against all damages and other liabilities arising out of our development activities or products produced in connection with these collaborations.

Item 3: Quantitative and Qualitative Disclosures About Market Risk

We are exposed to interest rate risk primarily through our investments in short-term marketable securities. Our investment policy calls for investment in short term, low risk instruments. As of September 30, 2003, investments in marketable securities were $300.8 million. Due to the nature of these investments, if market interest rates were to increase immediately and uniformly by 10% from levels as of September 30, 2003, the decline in the fair value of the portfolio would not be material.

We are exposed to equity price risks on the marketable portion of equity securities included in our portfolio of long-term investments. These investments are in small capitalization stocks in the pharmaceutical/biotechnology industry sector, and are primarily in companies with which we have research and development, licensing or other collaborative agreements. We typically do not attempt to reduce or eliminate our market exposure on these securities. As of September 30, 2003, long-term investments were $18.2 million.

We are exposed to foreign exchange rate fluctuations as the financial results of our foreign operations are translated into U.S. dollars in consolidation. As exchange rates vary, these results, when translated, may vary from expectations and adversely impact our financial position or results of operations. All of our revenues are denominated in U.S. dollars. We do not enter into forward exchange contracts as a hedge against foreign currency exchange risk on transactions denominated in foreign currencies or for speculative or trading purposes. If currency exchange rates were to fluctuate immediately and uniformly by 10% from levels as of September 30, 2003, the impact to our financial position or results of operations would not be material.

Item 4: Controls and Procedures

(a) ***Evaluation of disclosure controls and procedures.*** We maintain "disclosure controls and procedures," as such term is defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act"), that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Based on their evaluation as of the end of the period covered by this Quarterly Report on Form 10-Q, our Chief Executive Officer and Chief Financial Officer have concluded that, subject to the limitations noted above, our disclosure controls and procedures were effective to ensure that material information relating to us, including our consolidated subsidiaries, is made known to them by others within those entities, particularly during the period in which this Quarterly Report on Form 10-Q was being prepared.

(b) ***Changes in internal control over financial reporting***. There was no change in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) identified in connection with the evaluation described in Item 4(a) above that occurred during our last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II: OTHER INFORMATION

Item 1: Legal Proceedings

Invitrogen

On October 17, 2001, Invitrogen Corporation filed a complaint for patent infringement against Incyte in the United States District Court for the District of Delaware. On November 21, 2001, we filed our answer to Invitrogen's complaint. In addition, we asserted seven counterclaims against Invitrogen seeking declaratory relief with respect to the patents at issue, implied license, estoppel, laches, and patent misuse. We are also seeking our fees, costs, and expenses. Invitrogen filed its answer to our counterclaims on January 9, 2002. On February 25, 2003, we added a counterclaim for unfair business practices under California Business & Professions Code Section 17200. On June 24, 2003, the Court stayed all proceedings pending final disposition of the

appeal in the related case Clontech Laboratories, Inc. v. Invitrogen Corporation, C.A. No. 98-750-SLR (D. Del.), or entry of any order in any other action invalidating the same patents that are asserted in this case.

On November 21, 2001, we filed a complaint against Invitrogen, amended on December 21, 2001 and March 7, 2002, in the United States District Court for the Southern District of California alleging infringement of thirteen of its patents. Eight of the asserted patents (U.S. patent numbers 5,633,149, 5,637,462, 5,817,497, 5,840,535, 5,919,686, 5,925,542, 5,962,263, and 5,789,198) are gene patents. Three of the patents (U.S. patent numbers 5,716,785, 5,891,636, and 6,291,170) relate to RNA amplification and gene expression. Two of the patents (U.S. patent numbers 5,807,522 and 6,110,426) relate to methods of fabricating microarrays of biological samples. The complaint seeks a permanent injunction enjoining Invitrogen from further infringement of the patents at issue, damages for Invitrogen's conduct, as well as our fees, costs, and interest. We further seek triple damages based on Invitrogen's willful infringement of our patents. On April 2, 2002, Invitrogen filed its answer to our complaint and brought counterclaims against us seeking declaratory judgments that the patents in suit are invalid and not infringed. Invitrogen also pled, but later withdrew, its affirmative defense and counterclaim alleging that U.S. patent number 6,110,426 is unenforceable. On April 25, 2002, we filed our answer denying Invitrogen's counterclaims. Invitrogen has represented to the Court that its past sales of the eight GeneStorm cDNA clones charged with infringement of U.S. Patent Nos. 5,633,149, 5,637,462, 5,789,198, 5,817,497, 5,840,535, 5,919,686, 5,925,542 and 5,962,263 were not substantial and that it no longer sells these products. On July 2, 2003, the Court entered a stipulated two-month stay of all proceedings in this action. A stipulated two-month stay of all proceedings in this action was lifted on September 2, 2003. On October 2, 2003, this case was reassigned and the final pretrial conference in the case is scheduled for May 3, 2004.

Item 5: Other Information

Our 2004 Annual Meeting will be held on May 25, 2004 at such place and time as will be set forth in our proxy statement relating to that meeting. A stockholder proposal not included in the proxy statement for our 2004 Annual Meeting will be ineligible for presentation at the meeting unless the stockholder gives timely notice of the proposal in writing to the Secretary of Incyte at our principal executive offices and otherwise complies with the provisions of our Bylaws. To be timely, our Bylaws provide that we must have received the stockholder's notice not less than 60 days nor more than 90 days prior to the scheduled date of such meeting. However, if notice or prior disclosure of the date of the annual meeting is given or made to stockholders less than 70 days prior to the meeting date, we must receive the stockholder's notice by the earlier of (i) the close of business on the 10th day after the earlier of the day we mailed notice of the annual meeting date or provided such public disclosure of the meeting date and (ii) two days prior to the scheduled date of the annual meeting. For our 2004 Annual Meeting of Stockholders, stockholders must submit written notice to the Secretary in accordance with the foregoing Bylaw provisions no later than March 26, 2004.

Item 6: Exhibits and Reports on Form 8-K

a) Exhibits

Exhibit Number	Description of Document
31.1	Rule 13a – 14(a) Certification of Chief Executive Officer
31.2	Rule 13a – 14(a) Certification of the Chief Financial Officer
32.1*	Statement of the Chief Executive Officer under Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C Section 1350)
32.2*	Statement of the Chief Financial Officer under Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C Section 1350)

* In accordance with Item 601(b)(32)(ii) of Regulation S-K and SEC Release Nos. 33-8238 and 34-47986, Final Rule: Management's Reports on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports, the certifications furnished in Exhibits 32.1 and 32.2 hereto are deemed to accompany this Form 10-Q and will not be deemed "filed" for purpose of Section 18 of the Exchange Act. Such certifications will not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act, except to the extent that the registrant specifically incorporates it by reference.

b) Reports on Form 8-K

On July 30, 2003, we filed a Current Report on Form 8-K furnishing under Item 12 our press release relating to our financial results for the quarter ended June 30, 2003.

On September 8, 2003, we filed a Current Report on Form 8-K, under Item 5, announcing we had entered into a collaborative licensing agreement with Pharmasset, Ltd.

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.

INCYTE CORPORATION

Dated: November 13, 2003

By: /s/ PAUL A. FRIEDMAN

PAUL A. FRIEDMAN
Chief Executive Officer
(Principal Executive Officer)

Dated: November 13, 2003

By: /s/ DAVID C. HASTINGS

DAVID C. HASTINGS
Chief Financial Officer
(Principal Financial Officer)

INCYTE CORPORATION

EXHIBIT INDEX

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Exhibit 31.1

CERTIFICATION

I, Paul A. Friedman, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Incyte Corporation;
2. Based on my knowledge, this 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 report;
3. Based on my knowledge, the financial statements, and other financial information in this 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 report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and we have:
   a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, 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 report is being prepared;
   b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   c) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
   a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2003

/s/ PAUL A. FRIEDMAN

PAUL A. FRIEDMAN
Chief Executive Officer

Exhibit 31.2

CERTIFICATION

I, David C. Hastings, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Incyte Corporation;
2. Based on my knowledge, this 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 report;
3. Based on my knowledge, the financial statements, and other financial information in this 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 report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and we have:
   a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, 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 report is being prepared;
   b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   c) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
   a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 13, 2003

/s/ DAVID C. HASTINGS

DAVID C. HASTINGS
Chief Financial Officer

Exhibit 32.1

STATEMENT PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

With reference to the Quarterly Report of Incyte Corporation (the "Company") on Form 10-Q for the quarter ended September 30, 2003 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Paul A. Friedman, Chief Executive Officer of the Company, certify, for the purposes of 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

(1) the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ PAUL A. FRIEDMAN

PAUL A. FRIEDMAN
Chief Executive Officer
November 13, 2003

Exhibit 32.2

STATEMENT PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

With reference to the Quarterly Report of Incyte Corporation (the "Company") on Form 10-Q for the quarter ended September 30, 2003 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, David A. Hastings, Chief Financial Officer of the Company, certify, for the purposes of 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

(1) the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ DAVID C. HASTINGS

DAVID C. HASTINGS
Chief Financial Officer
November 13, 2003