Vertex Pharmaceuticals (Europe) Limited

Registered in England & Wales 2907620

Report and Financial Statements

31 December 2014

Directors

I F Smith
S Bedson
S K Lem

Secretary

Mitre Secretaries Limited

Auditors

Ernst & Young LLP
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Strategic Report

The directors present their strategic report for the year ended 31 December 2014.

Principal activity and review of the business

From 1 January, 2014 until 30 November, 2014 the principal activity of the company ('VPEL') was the development of the European pharmaceutical market and the performance of research on behalf of Vertex Pharmaceuticals Incorporated. From 30 November, 2014 the company was the owner of worldwide stock, non-North American intellectual property and began selling products through limited risk distributors in the UK and Ireland.

From 30 November, 2014 the company was supplying KALYDECO (also known as ivacaftor or VX-770), a novel therapy to treat the underlying cause of Cystic Fibrosis (CF). KALYDECO is a treatment for patients with CF six years of age and older who have the G551D mutation in their CFTR gene.

In the fourth quarter of 2015, the European Commission approved KALYDECO for patients with CF two to five years of age who have one of nine gating mutations in their CFTR gene and in patients with CF 18 years of age and older who have the R117H mutation in their CFTR gene.

In the fourth quarter of 2015, the European Commission approved ORKAMBI (ivacaftor in combination with lumacaftor or VX-809) for the treatment of patients with CF twelve years of age and older who are homozygous for the F508del mutation in their CFTR gene.

In the first quarter of 2015, the Vertex group initiated a Phase 3 development program for VX-661 in combination with ivacaftor in multiple CF patient populations who have at least one copy of the F508del mutation.

Reorganisation

In August 2014, the Vertex executive team under the direction of CEO Jeffrey Leiden evaluated locations outside of North America for the International headquarters. The team concluded that locating in the vicinity of the existing Research and Development (R&D) site in the UK was the ideal choice for Vertex moving forward. Other Vertex Group companies have been present in the UK for up to twenty years. Furthermore other factors were:

1) Access to developed labour markets and pools of talent within R&D, medical and commercial sectors.

2) World-class infrastructure with connections to the US and Europe.

3) Proximity to key Vertex vendor contractors involved in the supply chain including, but not limited to, Aesica, Arvato and Hovione.

The realignment of operations include:

- Moving the International headquarters from Switzerland to the UK
- Vertex Pharmaceuticals (Europe) Ltd. (VPEL) taking ownership of worldwide stock and oversight of manufacturing
- The migration of Non-North American Intellectual Property associated with the Cystic Fibrosis product profile

The management's opinion is that by realigning operations in the UK the company's legal structure will be simplified. This action also has the advantage of consolidating the company's manufacturing operations and provides a platform for future expansion.

The Vertex group commenced the reorganisation of its operations on 30 November, 2014. From that date, VPEL operates as the medicine development, supply chain and commercialization partner of Vertex Pharmaceuticals Inc. As a consequence VPEL was the parent company of Limited Risk Distributors (LRD's) operating in the UK and Ireland by 31 December, 2014.

Vertex Pharmaceuticals Inc. contributed the shares of Vertex Pharmaceuticals UK to Vertex Holdings in exchange for non-voting shares in Vertex Holdings. Vertex Holdings contributed the shares of Vertex Pharmaceuticals UK to VPEL in exchange for one thousand additional shares in VPEL.

Vertex Pharmaceuticals UK transferred all its assets and liabilities to VPEL at fair value in exchange for an intercompany promissory note. Vertex Pharmaceuticals UK was then classified as a non-trading entity.

Vertex Switzerland transferred the shares of Vertex Pharmaceuticals (Ireland) Limited to VPEL in exchange for an intercompany note. Vertex Pharmaceuticals (Ireland) Limited transferred its entire stock to VPEL in exchange for an intercompany promissory note.

The International Headquarters move from Switzerland to the UK happened on 6 July, 2015 concurrent with the opening of new offices in Paddington, London.

BioAxone

In October 2014, Vertex Pharmaceuticals Inc. (VPI) and VPEL entered into a license and collaboration agreement with BioAxone Biosciences, Inc., (or BioAxone), a privately-held biotechnology company. Vertex Pharmaceuticals is collaborating with BioAxone on the research, development and commercialization of VX-210 (formerly referred to as Cethrin), a biologic controlled by BioAxone, for the treatment of patients with spinal cord injuries. VX-210 is a Rho inhibitor, also described as a Rho antagonist, which the company believes has the potential to block inhibitory signalling, which may result in the regrowth and/or regeneration of axons after spinal injury. VX-210 has been evaluated as a single dose application in an open-label, non-placebo controlled Phase 1/2a clinical trial at multiple doses in 48 patients with thoracic and cervical acute spinal cord injuries. The company expect to commence a Phase 2b clinical trial of VX-210 in late 2015.

VPI and VPEL made initial payments of $6.5 million to BioAxone (70% by VPI and 30% by VPEL). BioAxone has the potential to receive up to $90.0 million in milestones and fees, including development and regulatory milestone payments and a license continuation fee, to which VPEL is also committed to contribute 30%. In addition, BioAxone would receive royalties and commercial milestones based on future net product sales, if any. VPI hold an option to purchase BioAxone at a predetermined price. The option expires at the earliest of (a) the day the FDA accepts a Biologics License Application submission for VX-210, (b) the day the company elects to continue the license instead of exercising the option to purchase BioAxone and (c) 15 March, 2018, subject to our option to extend this date by one year. The company may terminate its agreement with BioAxone upon 90 days' notice or immediately if it determines that a licensed product is unsafe for administration to humans. The agreement may also be terminated by either party for a material breach by the other or by BioAxone for our inactivity with respect to VX-210, in each case subject to notice and cure provisions. Unless earlier terminated, the agreement will continue until the expiration of our royalty obligations.

Financial Results

The results of the company's key financial and other performance indicators during the year were as follows:

	2014	*2013*	*Change*
	£m	*£m*	*%*
Turnover – Research and development cost plus arrangement	37.3	31.1	+19.9%
Turnover – Product sales	8.6	-	-
Research and development expenditure –Milton Park	31.2	-	-
R&D – Non-North American IP	7.3	-	-
R&D - Total	38.5	24.7	55.9%
Average number of research employees	107	109	(1.8%)

During 2014 the company's turnover from its research and development cost plus arrangement increased by 19.9%. Commercial activity commenced in December, 2014 as a result of the reorganisation referred to above. Hence, £8.6 million of product sales was recorded.

Research and development expenditure increased by 55.9% during the year. This is a result of increased investment in the Milton Park site and non-North American IP development costs.

The average number of research employees decreased by 1.8%, representing staff turnover and timing of new hires.

Principal risks and uncertainties

The company operates in a high-risk sector. The key risks facing the company are as follows:

Financial risks

A key area of exposure for the company is cash-flow risk. The company is wholly reliant on the liquidity of the parent organisation and its ability to provide the company with adequate funds for the foreseeable future. There is also an exchange rate risk related to purchases made in Euros and US Dollars whilst sales are made in £ Sterling, which could impact the planned expenditure by the ultimate parent.

Vertex Pharmaceuticals Incorporated, the company's ultimate parent undertaking, has indicated its intention to provide such ongoing financial support as is necessary for the company to continue in operation and to meet its liabilities as they fall due for at least 12 months from the date of approval of these financial statements. At 31 December 2014, the company had cash and bank balances of £13,637,000 and no external debt. Accordingly, the company has no significant interest rate exposure to manage locally.

Credit risks

In its current state of research and development activity in Europe, the company has no credit risk exposure with third party customers prior to November 2014. From December 2014 in addition to managing the research and development the company became a commercial trading entity and as such bears a credit risk, primarily in the UK and Republic of Ireland. The company sells to public institutions whereby the credit risk is deemed low as it is based on the sovereign risk of the country in which the institution operates.

Product and regulatory risks

The clinical development and commercial launch success of key drug candidates will depend on many factors. These include the timely completion and favourable outcome of clinical trials including achieving safety and efficacy end points, agreeing mutually acceptable scope and design of such clinical trials with relevant authorities, obtaining marketing and reimbursement access, establishing commercial manufacturing arrangements and gaining acceptance by the medical community for our products ahead of those developed by our competitors.

Stock

The Company has limited flexibility to adjust its supply in response to changes in demand, due to the significant lead times required to manufacture some of its products. Future adverse changes in the outlook for commercial sales could result in stock write downs and related charges.

On behalf of the Board

..... 15 December, 2015

Ian Smith, Director Date

Registered No. 2907620

Directors' report

The directors present their report for the year ended 31 December 2014.

Directors

The directors who served the company during the year and to date were as follows:

I F Smith
J M Leiden (resigned 5 October 2015)
S Bedson (appointed 5 October 2015)
S Lem (appointed 5 October 2015)

Results and dividends

The loss for the year after taxation amounted to £5,398,000 (2013 – loss of £898,000). The directors do not recommend a dividend for the year 2014 (2013 – £nil).

Future developments

The company has continued to expand and refurbish its laboratories and offices. The aim is to increase the Company's Research and Development capabilities in line with the Parent undertaking's corporate strategy. The company also entered into a new lease for an office in London during the first quarter of 2015. This office is the new headquarters of the non-North American Vertex operations. The funding requirements are being met by the Parent undertaking.

On 4 June, 2015, the Vertex Group entered into a strategic collaboration and license agreement (the "Parion Agreement") with Parion Sciences, Inc. ("Parion"). Pursuant to the agreement, the Company is collaborating with Parion to develop investigational epithelial sodium channel ("ENaC") inhibitors, including VX-371 (formerly P-1037) and P-1055, for the potential treatment of cystic fibrosis, or CF, and other pulmonary diseases. The Company is leading development activities for VX-371 and P-1055 in CF and other pulmonary diseases and is responsible for all costs, subject to certain exceptions, related to development and commercialization of the compounds.

Pursuant to the Parion Agreement, the Company has worldwide development and commercial rights to Parion's lead investigational ENaC inhibitors, VX-371 and P-1055, for the potential treatment of CF and all other pulmonary diseases and has the option to select additional compounds discovered in Parion's research program. Parion received an $80.0 million up-front payment (60% from VPEL and 40% from VPI) and has the potential to receive up to an additional (i) $490.0 million in development and regulatory milestone payments for development of ENaC inhibitors in CF, including $360.0 million related to global filing and approval milestones, (ii) $370.0 million in development and regulatory milestones for VX-371 and P-1055 in non-CF pulmonary indications and (iii) $230.0 million in development and regulatory milestones should the Company elect to develop an additional ENaC inhibitor from Parion's research program. The Company has agreed to pay Parion tiered royalties that range from the low double digits to mid-teens as a percentage of potential sales of licensed products.

The Company may terminate the Parion Agreement upon 90 days' notice to Parion prior to any licensed product receiving marketing approval or upon 180 days' notice after such point. Parion may terminate upon 30 days' notice if the Company experiences a change of control prior to the initiation of the first Phase 3 clinical trial for a licensed product, subject to the Company's right to receive specified royalties on any subsequent commercialization of licensed products. The Parion Agreement also may be terminated by either party for a material breach by the other, subject to notice and cure provisions. Unless earlier terminated, the agreement will continue in effect until the expiration of the Company's royalty obligations, which expire on a country-by-country basis on the later of (i) the date the last-to-expire patent covering a licensed product expires or (ii) ten years after the first commercial sale in the country.

Directors' report

In the third quarter of 2015 VPEL acquired the wholesale distribution licences for export markets where the Vertex group does not have a limited risk distributor (LRD) or the LRD does not have the appropriate licence. During 2015, further LRD's in Austria, Portugal, Sweden & Switzerland were established as subsidiaries of VPEL.

On 26 October, 2015, the Company entered into a strategic collaboration, option and license agreement (the "CRISPR Agreement") with CRISPR Therapeutics AG and its affiliates ("CRISPR") to collaborate on the discovery and development of potential new treatments aimed at the underlying genetic causes of human diseases using CRISPR-Cas9 gene editing technology. The Company has the exclusive right to license up to six CRISPR-Cas9-based targets. In connection with the CRISPR Agreement, the Company made an upfront payment to CRISPR of $75.0 million and will make a $30.0 million investment in CRISPR pursuant to a convertible loan agreement.

The Company will fund the entire discovery activities conducted pursuant to the CRISPR Agreement. For potential hemoglobinapathy treatments, including treatments for sickle cell disease, the Company and CRISPR will share equally all research and development costs and worldwide revenues. For other targets that the Company elects to license, the Company would lead all development and global commercialization activities. For each of up to six targets that the Company elects to license, other than hemoglobinapathy targets, CRISPR has the potential to receive up to $420.0 million in development, regulatory and commercial milestones and royalties on net sales.

The Company may terminate the CRISPR Agreement upon 90 days' notice to CRISPR prior to any product receiving marketing approval or upon 270 days' notice after such point. The CRISPR Agreement also may be terminated by either party for a material breach by the other, subject to notice and cure provisions. Unless earlier terminated, the CRISPR Agreement will continue in effect until the expiration of the Company's payment obligations under the CRISPR Agreement.

Going concern

Vertex Pharmaceuticals Incorporated, the company's ultimate parent undertaking, has indicated its intention to provide such ongoing financial support as is necessary for the company to continue in operation and to meet its liabilities as they fall due for at least 12 months from the date of approval of these financial statements.

After making enquiries, the directors have a reasonable expectation that the company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

Research and development activities

The company performs research and development on behalf of the parent undertaking, Vertex Pharmaceuticals Incorporated. During the year the company incurred expenditure of £31.2 million (2013 – £24.7 million) on research and development, which was all expensed to the profit and loss account. In addition, amounts payable to VPI in December 2014, for VPEL's share of development costs of the non-North American IP acquired on 30 November, 2014 totalled £7.3 million.

Directors' liabilities

The company has granted an indemnity to one or more of its directors against liability in respect of proceedings brought by third parties, subject to the conditions set out in section 234 of the Companies Act 2006. Such qualifying third party indemnity provision remains in force as at the date of approving the directors' report.

Directors' report

Disclosure of information to the auditors

So far as each person who was a director at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with preparing its report, of which the auditor is unaware. Having made enquiries of fellow directors and the company's auditor, each director has taken all the steps that he/she is obliged to take as a director in order to make himself/herself aware of any relevant audit information and to establish that the auditor is aware of that information.

Auditors

A resolution to reappoint Ernst & Young LLP as auditors will be put to the members at the Annual General Meeting.

On behalf of the Board

..... 15 December 2015

Ian Smith, ~~Director~~ Date

Statement of directors' responsibilities

The directors are responsible for preparing the Strategic report, the Directors' report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Independent auditor's report

To the members of Vertex Pharmaceuticals (Europe) Limited

We have audited the financial statements of Vertex Pharmaceuticals (Europe) Limited for the year ended 31 December 2014 which comprise the Profit and Loss Account, the Statement of Total Recognised Gains and Losses, the Balance Sheet and the related notes 1 to 26. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 9, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the report and financial statements to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on the financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 December 2014 and of its loss for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Independent auditor's report

To the members of Vertex Pharmaceuticals (Europe) Limited

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Ernst & Young LLP

.....

Ian Oliver (senior statutory auditor)
For and on behalf of Ernst & Young LLP (Statutory Auditor)
Reading

18 December 2015

Profit and loss account

for the year ended 31 December 2014

	Notes	2014			2013
		£'000	£'000	£'000	£'000
		Acquisitions	Ongoing Business	Total	
Turnover	2	8,590	37,334	45,924	31,147
Cost of sales		(4,882)	–	(4,882)	–
Gross Profit		3,708	37,334	41,042	31,147
Research and development expenditure		–	(38,461)	(38,461)	(24,706)
Administrative expenses		(651)	(8,531)	(9,182)	(7,103)
Other income		–	1,766	1,766	–
Operating Profit/(Loss)	3	3,057	(7,892)	(4,835)	(662)
Interest receivable and similar income	6			12	12
Interest payable and similar charges	7			(341)	(248)
Loss on ordinary activities before tax				(5,164)	(898)
Tax on loss on ordinary activities	8			(234)	–
Loss for the financial year	18			(5,398)	(898)

All amounts relate to continuing activities.

Statement of total recognised gains and losses

for the year ended 31 December 2014

There are no recognised gains or losses other than the loss attributable to the shareholders of the company of £5,398,000 in the year ended 31 December 2014 (2013 – loss of £898,000).

Balance sheet

at 31 December 2014

	Notes	2014 £'000	2013 £'000
Fixed assets			
Intangible assets	9	965,680	-
Tangible fixed assets	10	24,207	18,175
Investment in subsidiaries	11	31,309	-
		1,021,196	18,175
Current assets			
Stock	12	20,593	-
Debtors – due within one year	13	63,945	3,863
– due after more than one year	13	1,728	245
		65,673	4,108
Cash at bank and in hand		13,637	1,980
		99,903	6,088
Creditors: amounts falling due within one year	14	(87,931)	(9,410)
Net current assets/(liabilities)		11,972	(3,322)
Total assets less current liabilities		1,033,168	14,853
Creditors: amounts falling due after more than one year	15	(69,439)	(5,888)
Provisions for liabilities	16	(6,271)	(2,827)
Net assets		957,458	6,138
Capital and Reserves			
Called up share capital	17	128	125
Capital contribution	18	6,000	6,000
Share premium account	18,19	957,347	-
Accumulated (loss) / profit	18	(6,017)	13
Shareholders' funds	18	957,458	6,138

The financial statements of Vertex Pharmaceuticals (Europe) Limited were approved for issue by the Board of Directors on:

15 December 2015

Ian Smith, Director

15 December 2015

Date

Notes to the financial statements

at 31 December 2014

1. Accounting policies

Basis of preparation

The financial statements are prepared under the historical cost convention and in accordance with applicable accounting standards.

Going concern

The financial statements are prepared on the going concern basis as the parent undertaking, Vertex Pharmaceuticals Incorporated, the ultimate parent, has indicated its intention to provide such financial support as is necessary for the company to continue in operation and to meet its liabilities as they fall due for at least 12 months from the date of approval of these financial statements.

Group financial statements

The financial statements present information about the company as an individual undertaking and not about its group. The company is exempt under section 402 of the Companies Act 2006 from preparing group financial statements on the basis that it is a wholly owned subsidiary of Vertex Pharmaceuticals, Incorporated, and its ultimate parent publishes group financial statements.

Turnover

Turnover includes amounts receivable as services are provided to Vertex Pharmaceuticals Incorporated, the company's parent undertaking based in the USA, under the terms of a service agreement whereby the company provides market development and direct research on behalf of its parent undertaking. All amounts are exclusive of discounts and value added tax.

Turnover from the sale of goods is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer, usually on dispatch of the goods.

For the month of December 2014, as Vertex Pharmaceuticals (Europe) Limited could not legally sell to third parties because of the lack of a Wholesale Distribution Licence, Vertex Pharmaceuticals (UK) Limited and Vertex Pharmaceuticals (Ireland) Limited entered into an intercompany agreement with Vertex Pharmaceuticals (Europe) Limited to continue to sell into its local markets on behalf of Vertex Pharmaceuticals (Europe) Limited.

Stock

VPEL ('the company') values its stock at the lower of cost or market value. The Company determines the cost of its stock, which includes amounts related to materials and manufacturing overhead, on a first-in, first –out basis. If the company identifies excess, obsolete or unsalable items, its stocks are written down to their realisable value in the period in which the impairment is first identified. Shipping and handling costs incurred for stock purchases and product shipments are recorded in cost of sales in the company's profit and loss account.

The company capitalises stock produced in preparation for initiating sales of a drug candidate when the related drug candidate is considered to have a high likelihood of regulatory approval and the related costs are expected to be recoverable through sales of the stock. In determining whether or not to capitalise such stock, the company evaluates, among other factors, information regarding the drug candidate's safety and efficacy, the status of regulatory submissions and communications with the regulatory authorities and the outlook for commercial sales, including the existence of current or anticipated competitive drugs and the availability of reimbursement. In addition, the company evaluates risks associated with manufacturing the drug candidate and the remaining shelf life of the stock items.

Notes to the financial statements

at 31 December 2014

Statement of cash flows

The company is a wholly owned subsidiary of Vertex Pharmaceuticals Incorporated and the cash flows of the company are included in the group statement of cash flows of Vertex Pharmaceuticals Incorporated. The group financial statements of Vertex Pharmaceuticals Incorporated are publicly available. Consequently, the company is exempt under the terms of FRS 1 (revised 1996), 'Statement of Cash Flows', from publishing a statement of cash flows.

Intangible Assets

Intangible assets acquired separately from a business are capitalised at cost. Intangible assets acquired as part of an acquisition of a business are capitalised separately from goodwill if the fair value can be measured reliably on initial recognition, subject to the constraint that, unless the asset has a readily ascertainable market value, the fair value is limited to an amount that does not create or increase any negative goodwill arising on the acquisition. Intangible assets, excluding development costs, created within the business are not capitalised and expenditure is charged against profits in the year in which it is incurred.

Intangible assets available for use are amortised on a straight line basis over their estimated useful life. The carrying value of intangible assets is reviewed for impairment on an annual basis and more frequently if events or changes in circumstances indicate the carrying value may not be recoverable.

The company's intangible assets include Non-North American IP rights. Vertex Pharmaceuticals (Europe) Limited has assumed Vertex Cayman's role as a cost sharing participant with Vertex US for the development of the Cystic Fibrosis compounds.

The intangible assets represent a non-exclusive licence to exploit the ex-North American Intellectual Property (IP) related to the Cystic Fibrosis franchise, including VX-809, VX-770 and VX-661. The licence fair value is based upon the net present value of future cash flows from revenues through to patent expiration which is 31 December 2026. Therefore, rights to VX-770 are amortised on a straight line basis over their estimated useful lives of 12 years. Rights to VX-809 and VX-661 have not commenced amortisation as the product candidates are under development and not yet available for use.

Goodwill

The difference between the purchase price and the fair value of assets acquired and liabilities assumed in a business combination is allocated to goodwill. Positive goodwill arising on acquisitions is capitalised, classified as an asset on the balance sheet and amortised on a straight line basis over its useful economic life. Goodwill is evaluated for impairment on an annual basis, and more frequently if indicators are present or changes in circumstances suggest that impairment may exist.

Tangible fixed assets

The cost of tangible fixed assets is their purchase cost, together with any incidental costs of acquisition.

Depreciation is calculated so as to write off the cost of tangible fixed assets, less their estimated residual values, over the expected useful economic lives of the assets concerned. The principal annual rates and methods used for this purpose are:

Short leasehold improvements	–	Spread over lease term (5-15 years) - straight-line
Plant and machinery	–	14% - straight-line
Fixtures, fittings and equipment	–	25% - straight-line
Computer hardware and software	–	33 1/3% - straight-line

Notes to the financial statements

at 31 December 2014

The carrying values of tangible fixed assets are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable.

Assets under construction are not depreciated until they are available for use.

Investments

Details of the investments in which the company holds 20% or more of the nominal value of any class of share capital are as follows:

Subsidiary undertakings:

Name of company	Holding	Proportion of voting rights and shares held	Nature of business
Vertex Pharmaceuticals (UK) Limited	Ordinary shares	100%	Distribution of small molecule drugs
Vertex Pharmaceuticals (Ireland) Limited	Ordinary shares	100%	Distribution of small molecule drugs

Investments in subsidiaries are accounted for at the lower of cost and net realisable value.

The carrying values of investments recorded at cost are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. Impairment is measured by comparing the carrying value of the investment with its recoverable amount (the higher of net realisable value and value in use). To the extent that the carrying amount exceeds the recoverable amount, the investment is impaired and is written down. The impairment loss is recognised in the profit and loss account.

Provisions

A provision is recognised when the group has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation.

Provisions for property dilapidations are discounted at 1.56% p.a. as the leases expire in 2024. Provisions for national insurance are not discounted.

Research and development

Research and development expenditure is written off to the profit and loss account as it is incurred.

Deferred taxation

Deferred taxation is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events have occurred at that date that will result in an obligation to pay more, or right to pay less or to receive more, tax, with the following exception:

- Deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax is measured on an undiscounted basis at the tax rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date.

Notes to the financial statements

at 31 December 2014

Research and development expenditure credits (above the line) to be received in cash are recorded in other income in the period in which qualifying expenditure was incurred.

Foreign currencies

Transactions denominated in foreign currencies are translated at the rate of exchange ruling at the date of the transaction. All foreign currency balances outstanding at the balance sheet date are retranslated at rates of exchange ruling on that date. All exchange differences are taken to the profit and loss account in the period in which they arise.

Operating leases

Rentals payable under operating leases are charged on a straight line basis over the lease term. Lease incentives are recognised over the shorter of the lease term and the date of the next rent review.

Pensions

The company makes contributions to defined contribution pension schemes. The assets of these schemes are held separately from those of the company in independently administered funds. The pension cost represents contributions payable by the company to the schemes during the year.

Share-based payments

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted and is recognised as an expense over the vesting period, which ends on the date on which the relevant employees become fully entitled to the award. Fair value is determined using an appropriate pricing model. In valuing equity-settled transactions, no account is taken of any vesting conditions, other than conditions linked to the price of the shares of the company (market conditions).

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

At each balance sheet date before vesting, the cumulative expense is calculated, representing the extent to which the vesting period has expired and management's best estimate of the achievement or otherwise of non-market conditions and the number of equity instruments that will ultimately vest or in the case of an instrument subject to a market condition, be treated as vesting as described above. The movement in cumulative expense since the previous balance sheet date is recognised in the profit and loss account, with a corresponding entry in equity.

Charges received from the parent undertaking in respect of the share-based payment scheme are reversed out of the result for the year and treated as a distribution in the reconciliation of shareholders' funds.

In accordance with UITF25 the company provides for the National Insurance that would become payable on outstanding share-based payment arrangements awarded under unapproved schemes. The provision is calculated on the difference between the year-end share price of Vertex Pharmaceuticals Incorporated stock and the exercise price of outstanding share awards, and is being allocated over the relevant vesting periods.

Notes to the financial statements

at 31 December 2014

2. Turnover

	2014	*2013*
	£'000	*£'000*
United States of America	37,334	31,147
Rest of World	8,590	-
Total	45,924	31,147

3. Operating Loss

This is stated after charging/ (crediting):

	2014	*2013*
	£'000	*£'000*
Auditors' remuneration – audit of the financial statements	20	20
tax compliance services	3	3
Depreciation	3,807	3,788
Amortisation of goodwill and Intellectual Property (IP) rights	1,771	-
Loss on disposal of fixed assets	-	4
Foreign exchange loss / (gain)	1,230	(89)
Research and development expenditure	38,461	24,706
Operating lease rentals – land and buildings	1,206	1,243
Other income	(1,766)	-

The other income includes research and development expenditure credit (above the line) of £1,766,000 for 2013 and 2014. The amount in respect of 2013 was not recorded in the 2013 profit and loss account as the Scheme was newly introduced and the Company was awaiting confirmation that its activities and expenditure qualified.

4. Directors' remuneration

The directors are also directors or officers of a number of companies within the Vertex Pharmaceuticals Incorporated group. These directors' services to the company do not occupy a significant amount of time. As such these directors do not consider that they have received any remuneration in the current or prior year for these incidental services to the company.

During the year no director exercised share options (2013 – nil).

Notes to the financial statements

at 31 December 2014

5. Staff costs

	2014	*2013*
	£'000	*£'000*
Wages and salaries	15,109	12,686
Social security costs	3,514	3,848
Other pension costs (note 19)	696	666
	19,319	17,200

Wages and salaries include employee share-based payment expenses of £5,066,000 (2013 – £3,561,000).

The average monthly number of employees (including executive directors) during the year was made up as follows:

	No.	*No.*
Sales and administration	35	35
Research and development	107	109
	142	144

6. Interest receivable and similar income

	2014	*2013*
	£'000	*£'000*
Interest receivable on bank deposits	12	12
	12	12

7. Interest payable and similar charges

	2014	*2013*
	£'000	*£'000*
Interest payable on intercompany loan from parent undertaking	213	248
Interest payable on promissory notes	109	-
Interest accretion expense	19	-
	341	248

Notes to the financial statements

at 31 December 2014

8. Tax

(a) Tax on loss on ordinary activities

The tax is made up as follows:

	2014	*2013*
	£'000	*£'000*
Current tax:		
UK corporation tax on the loss for the year	234	–
Under/(over) provision in prior years	–	–
Total current tax (note 8(b))	234	–
Deferred tax:		
Origination and reversal of timing differences	–	–
Tax on loss on ordinary activities	–	–

(b) Factors affecting current tax loss for the year

The tax assessed for the year differs from the standard rate of corporation tax in the UK of 21.5% (2013 – 23.25%). The differences are explained below:

	2014	*2013*
	£'000	*£'000*
Loss on ordinary activities before tax	(5,164)	(898)
Loss on ordinary activities multiplied by standard rate of corporation tax in the UK of 21.5% (2013 – 23.25%)	(1,110)	(209)
Effects of:		
Research and development tax relief	(146)	(835)
Expenses not deductible for tax purposes	5	2
Decelerated/(accelerated) capital allowances	643	709
Other timing differences	1	3
Share-based payment: Schedule 23 relief	(535)	(1,565)
Current year losses carried forward	702	1,770
Carry forward of RDEC generated	234	-
Losses surrendered as group relief	440	125
Current tax for the year (note 8(a))	234	-

Notes to the financial statements

at 31 December 2014

8. Tax (continued)

(c) Deferred tax

Unrecognised deferred tax (assets) and liabilities comprise:

	2014	*2013*
	£'000	*£'000*
Trading losses	(4,288)	(5,119)
RDEC carry-forward	(234)	-
Other short-term timing differences	(70)	(571)
Decelerated capital allowances	261	864
	(4,331)	(4,826)

The deferred tax asset has not been recognised as there is insufficient evidence that the asset will be recovered. The asset would be recovered if there are any future profits of the same trade against which the trading losses can be offset.

(d) Factors that may affect future tax charges

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period when the asset is realised or the liability settled, based on tax rates that have been enacted or substantively enacted at the statement of financial position date.

The Finance Act 2013 was substantively enacted in July 2013 and included a reduction in the main rate of UK Corporation Tax to 21% from 1 April 2014 and to 20% from 1 April 2015. As these reductions to the rate were substantively enacted at the balance sheet date, the company has calculated deferred tax applying the rate at which it is expected the assets or liabilities will be realised i.e. deferred tax assets have been calculated at a rate of 20%.

The UK government intends to reduce the UK corporate income tax rate further, to 19% by 1 April 2017 and 18% by 1 April 2020, which will be enacted in subsequent Finance Bills. Consequently, the Company will only recognise the impact of the rate change which is substantively enacted at that time in its financial statements. The further reduction in tax rate will affect both the future current and deferred tax charge of the Company.

The impact of the proposed reduction from 20% to 18% would reduce the unrecognised deferred tax asset from £4,331k to £3,898k.

Notes to the financial statements

at 31 December 2014

9. Intangible assets

	Intellectual Property (IP) Rights	*Goodwill*	*Total*
	£'000	*£'000*	*£'000*
Cost:			
At 1 January 2014	–	–	–
Addition during the year (Non North American IP rights)	946,730	–	946,730
Addition during the year (BioAxone IP)	1,202	–	1,202
Goodwill on acquisition	-	19,519	19,519
At 31 December 2014	947,932	19,519	967,451
Amortisation:			
At 1 January 2014	–	–	–
Provided during the year	1,636	135	1,771
At 31 December 2014	1,636	135	1,771
Net book value at 31 December 2014	946,296	19,384	965,680
Net book value at 1 January 2014	–	–	–

The amortisable basis for ex-North American IP represents a non-exclusive licence to exploit the Cystic Fibrosis franchise, including VX-809, VX-770 and VX-661. The licence value is based upon the net present value of future cash flow from revenues through to patent expiry in 31 December 2026. VX-770 was the only product with market approval at the end of the year and is consequently being amortised on a straight line basis over its estimated useful life of 12 years. The other products were not available for use, therefore amortisation had not commenced at the end of 2014.

VPEL contributed $1.95m (£1.2m) to enter the BioAxone agreement. The products are in an early stage of development and are not yet available for use. As a result no amortisation has been recognised in the accounts.

The goodwill relates to the acquisition of the business, assets and liabilities of Vertex Pharmaceuticals (UK) Limited. Goodwill is amortised over the estimated useful economic life of KALYDECO (VX-770) of 12 years.

Notes to the financial statements

at 31 December 2014

On 30 November 2014 Vertex Pharmaceuticals (Europe) Ltd acquired the business, assets and liabilities of Vertex Pharmaceuticals (UK) Limited in exchange for a Promissory note. This was part of Vertex Pharmaceuticals Incorporated EU realignment project to combine its worldwide manufacturing, early development and UK commercial operations.

The acquisition is analysed as follows:

Net assets acquired:	**£000**
Cash	6,034
Debtors	10,921
Stock	886
Prepayments and deposits	51
Trade creditors	(98)
Accruals and deferred income	(1,817)
Other taxes and social security costs	(79)
VAT payable	(1,146)
Provisions	(27)
Amounts owed to group undertakings	(9,976)
Net assets acquired	4,749
Goodwill	19,519
Cost of acquisition	24,268
Discharged by:	
Promissory note due to Vertex Pharmaceuticals (UK) Limited	24,268

As part of the realignment, the Wholesale Distribution Licence (WDL) held by Vertex Pharmaceuticals (UK) Limited would have to be transferred to Vertex Pharmaceuticals (Europe) Limited. Vertex began working with a third party consultant to effectuate this change, and Vertex Pharmaceuticals (Europe) Limited obtained the license in August 2015.

For the month of December 2014, as Vertex Pharmaceuticals (Europe) Limited could not legally sell to third parties because of the lack of the WDL, Vertex Pharmaceuticals (UK) Limited entered into an intercompany agreement with Vertex Pharmaceuticals (Europe) Limited to continue to sell into its local markets on behalf of Vertex Pharmaceuticals (Europe) Limited.

Notes to the financial statements

at 31 December 2014

10. Tangible fixed assets

	Assets under construction £'000	*Plant & machinery* £'000	*Short leasehold improvements* £'000	*Fixtures, fittings and equipment* £'000	*Total* £'000
Cost:					
At 1 January 2014	-	-	23,634	15,492	39,126
Additions	1,764	4,804	2,786	485	9,839
Disposals	-	-	-	(419)	(419)
At 31 December 2014	1,764	4,804	26,420	15,558	48,546
Depreciation:					
At 1 January 2014	-	-	8,899	12,052	20,951
Charge for the year	-	56	2,157	1,594	3,807
Disposals	-	-	-	(419)	(419)
At 31 December 2014	-	56	11,056	13,227	24,339
Net book value:					
At 31 December 2014	1,764	4,748	15,364	2,331	24,207
At 1 January 2014	-	-	14,735	3,440	18,175

11. Investment in subsidiaries

	2014 £'000	*2013* £'000
At 1 January, 2014	-	-
Investment in shares of Vertex Pharmaceuticals (Ireland) Ltd.	31,308	-
Investment in shares of Vertex Pharmaceuticals (UK) Ltd.	1	-
At 31 December, 2014	31,309	-

VPEL purchased 100% of the shares of Vertex Pharmaceuticals (Ireland) Ltd. in return for a promissory note of £ 31.3 million.

VPEL acquired Vertex Pharmaceuticals (UK) Ltd. in return for 1,000 ordinary shares of £1 each.

Notes to the financial statements

at 31 December 2014

12. Stock

	2014	*2013*
	£'000	*£'000*
Raw materials	5,439	-
Work in progress	13,114	-
Finished goods	2,040	-
	20,593	-

During the year VPEL acquired stock from Vertex Pharmaceuticals (Ireland) Ltd. In the opinion of the directors, the current replacement cost does not differ significantly from the above amounts.

13. Debtors

	2014	*2013*
	£'000	*£'000*
Amounts falling due within one year:		
Trade debtors	11,587	15
Amounts owed by group companies	48,822	1,434
Corporation tax receivable	1,215	-
VAT recoverable	289	321
Prepayments and accrued income	2,032	2,093
	63,945	3,863
Amounts falling due after more than one year:		
Accrued income	1,728	245
	65,673	4,108

14. Creditors: amounts falling due within one year

	2014	*2013*
	£'000	*£'000*
Trade creditors	1,791	411
Amounts owed to group companies	70,510	4,938
Other taxation and social security costs	3,454	599
Accruals and deferred income	12,176	3,462
	87,931	9,410

Notes to the financial statements

at 31 December 2014

15. Creditors: amounts falling due after more than one year

	2014	*2013*
	£'000	*£'000*
Promissory note with Vertex Pharmaceutical (UK) Ltd	24,268	-
Promissory note with Vertex Pharmaceutical (Ireland) Ltd	13,842	-
Promissory note with Vertex Pharmaceutical (Switzerland) Sarl	31,308	-
Amounts owed to group undertakings	21	5,888
Total amount owed to group undertakings	69,439	5,888
Aggregate amount repayable after more than five years	69,418	-

Vertex Pharmaceuticals (UK) Limited transferred all of its assets and liabilities to Vertex Pharmaceuticals (Europe) Ltd in exchange for an intercompany promissory note (£24.3 million). Interest is payable at 1.89% per annum and the balance of this note together with any accrued interest will be due and payable in full on 31 December 2021.

Vertex Pharmaceuticals (Ireland) Limited transferred its stock to Vertex Pharmaceuticals (Europe) Ltd in exchange for an intercompany promissory note (£13.84 million). Interest is payable at 1.89% per annum and the balance of this note together with any accrued interest will be due and payable in full on 31 December 2021.

Vertex Pharmaceutical (Switzerland) Sarl transferred shares in Vertex Pharmaceuticals (Ireland) Limited to Vertex Pharmaceuticals (Europe) in exchange for an intercompany promissory note (£31.30 million). Interest is payable at 1.89% per annum and the balance of this note together with any accrued interest will be due and payable in full on 31 December 2021.

The amount owed to group undertakings is a loan from Vertex Pharmaceuticals Incorporated bearing an interest rate of 4.25% p.a. and is repayable in full on 24 March, 2016. This loan was partially repaid during the year.

16. Provisions for liabilities

	National insurance on share option gains	*Property dilapidations*	*Total*
	£'000	£'000	£'000
At 1 January 2014	1,493	1,334	2,827
Increase/ charge	881	2,517	3,398
Business acquisition	27	-	27
Interest accretion	-	19	19
At 31 December 2014	2,401	3,870	6,271

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National insurance on share option gains

Provision has been made for National Insurance contributions on those options awarded under unapproved share options schemes which are expected to be exercised. The amount of National Insurance payable depends upon the number of employees who remain with the company and exercise their options, the market price of the Vertex Pharmaceuticals Incorporated shares at the time of exercise and the prevailing National Insurance rates at the time. The provision takes into account the above factors and the movements in the market value of the Vertex Pharmaceuticals Incorporated shares to 31 December 2014.

Under an additional restricted share scheme employees are granted restricted shares in Vertex Pharmaceuticals Incorporated. These shares vest to the employee on an annual basis over a fixed period, where upon cessation of employment, the employee forfeits any unvested shares. For the restricted share scheme, the company is liable to pay National Insurance on the market value at the time the shares vest to the employee unless the employee has elected to pay taxation and National Insurance at the date the shares are granted in which case the employers' National Insurance is liable at this date.

Potential National Insurance on these share based payments was also included in the provision.

Property dilapidations

The dilapidations provision is based on the future expected repair costs required to restore the leased properties to their original condition at the end of their respective lease terms.

The Milton Park leases were renegotiated in 2015 and contractual amounts are due to be incurred at the end of the lease terms in 2024.

17. Called up share capital

		2014		*2013*
Allotted, called up and fully paid	*No.*	*£*	*No.*	*£*
Shares in issue at 1 January	125,000	125,000	125,000	125,000
New shares issued during the year	3,000	3,000	-	-
Ordinary shares of £1 each at 31 December	128,000	128,000	125,000	125,000

Notes to the financial statements

at 31 December 2014

18. Reconciliation of shareholders' funds and movements on reserves

	Share capital £'000	*Accumulated (loss)/profit £'000*	*Capital contribution £'000*	*Share premium account £'000*	*Total share-holders' funds £'000*
At 1 January 2013	125	376	6,000	-	6,501
Loss for the year	–	(898)	–	–	(898)
Share-based payment transactions	–	3,561	–	–	3,561
Parent undertaking charge for share-based payment transactions	–	(3,026)	–	–	(3,026)
At 31 December 2013	125	13	6,000	–	6,138
Shares issued in return for IP rights (see note 9)	1	–	–	946,734	946,735
Shares issued to acquire Vertex Pharmaceuticals (UK) Limited (see note 11)	1	–	–	–	1
Shares issued for intercompany consideration	1	–	–	10,613	10,614
Loss for the year	–	(5,398)	–	–	(5,398)
Share-based payment transactions	–	5,066	–	–	5,066
Parent undertaking charge for share-based payment transactions	–	(5,698)	–	–	(5,698)
At 31 December 2014	128	(6,017)	6,000	957,347	957,458

19. Share premium account

The share premium account records the amount above the nominal value received for shares issued, less transaction costs. In accordance with Section 610 of the Companies Act 2006, the share premium account is not distributable but can be used to write-off the expenses of the issue of those shares; to write off any commissions paid on the issue of those shares; or to pay up new shares to be allotted to members as fully paid bonus shares.

20. Pensions

The company operates a defined contribution pension scheme for its employees. Contributions for the year ended 31 December 2014 amounted to £694,000 (2013 – £666,000). Outstanding contributions at 31 December 2014 were £62,000 (2013 – £53,000). This amount is included within accruals.

Notes to the financial statements

at 31 December 2014

21. Other financial commitments

At 31 December 2014 the company had annual commitments under non-cancellable operating leases as set out below:

	2014 *Land and buildings* *£'000*	*2013* *Land and buildings* *£'000*
Operating leases which expire:		
Within one year	-	-
In two to five years	-	180
Over five years	749	934
	749	1,114

The annual amount is payable after a rent free period up to 30 September 2015.

Other commitments

BioAxone has the potential to receive up to $90.0 million in milestones and fees, including development and regulatory milestone payments and a license continuation fee, to which VPEL is also committed to contribute 30%. In addition, BioAxone would receive royalties and commercial milestones based on future net product sales, if any. VPI hold an option to purchase BioAxone at a predetermined price. The option expires at the earliest of (a) the day the FDA accepts a Biologics License Application submission for VX-210, (b) the day the company elects to continue the license instead of exercising the option to purchase BioAxone and (c) 15 March, 2018, subject to the company's option to extend this date by one year. The company may terminate our agreement with BioAxone upon 90 days' notice or immediately if the company determines that a licensed product is unsafe for administration to humans. The agreement may also be terminated by either party for a material breach by the other or by BioAxone for the company's inactivity with respect to VX-210, in each case subject to notice and cure provisions. Unless earlier terminated, the agreement will continue until the expiration of our royalty obligations.

22. Share premium account

The share premium account records the amount above the nominal value received for shares issued, less transaction costs. In accordance with Section 610 of the Companies Act 2006, the share premium account is not distributable but can be used to write-off the expenses of the issue of those shares; to write off any commissions paid on the issue of those shares; or to pay up new shares to be allotted to members as fully paid bonus shares.

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23. Share-based payments

Employee share purchase plan (ESPP)

The parent undertaking operates an employee share purchase plan, where all company employees have the opportunity to save between 1-15% of their gross monthly salary, the sum of which is used to purchase shares at six monthly intervals, May and November, at a discounted price. The share price of the purchase is calculated at a 15% discount on the lower of the average daily rate of the anchor price and the purchase date price.

During 2013 and 2014, the following shares were issued to company employees under the ESPP:

	2014	*2013*
Number of shares	17,882	22,459
Average price paid	US$53.75	US$35.36

Employee share purchase plan (ESPP) (continued)

The weighted average fair value of each purchase right granted to company employees during 2014 and 2013 was US$90.56 and US$70.24 respectively. The following table reflects the weighted average assumptions used in the Black-Scholes valuation model for 2014 and 2013:

	2014	*2013*
Expected stock price volatility (%)	60.32	54.69
Risk-free interest rate (%)	0.09	0.08
Expected term	0.75 years	0.74 years
Expected annual dividends	Nil	nil

The expected stock price volatility for ESPP offerings is based on implied volatility. The company bases the risk-free interest rate on the interest rate payable on U.S Treasury securities in effect at the time of grant for a period that is commensurate with the assumed expected term. The expected term represents purchases and purchase periods that take place within the offering period. The expected annual dividends estimate is nil because the company has not historically paid, and does not for the foreseeable future intend to pay, a dividend.

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23. Share-based payments (continued)

Stock options

The parent undertaking awards equity-settled stock options to company employees at the discretion of the compensation committee, managed by the ultimate parent. The options vest on a quarterly basis for a period of either 5 years (pre December 2003) or 4 years. An employee has 90 days upon leaving the company to exercise vested options.

The following table illustrates the number and weighted average exercise prices (WAEP) of, and movements in, share options during the year.

	2014	*2014*	*2013*	*2013*
		WAEP		*WAEP*
	No.	*US$*	*No.*	*US$*
Outstanding as at 1 January, 2014	496,165	45.33	709,234	37.20
Granted during the year	120,375	87.46	178,210	55.32
Forfeited during the year	(36,118)	(56.57)	(82,620)	(45.17)
Exercised	(197,165)	(42.01)	(308,659)	(32.83)
Transferred in due to business acquisition	12,857	67.81	-	-
Outstanding at 31 December, 2014	396,114	59.48	496,165	45.33
Exercisable at 31 December, 2014	152,027	48.13	175,330	38.57

The weighted average fair value per share of options granted to company employees during the year was US$41.19 (2013 – US$24.61). The weighted average remaining contractual life for options outstanding at the end of the year was 7.78 years (2013 – 7.30 years).

The range of exercise prices for share options outstanding at the end of the year were:

Range of Exercise Prices:	*Number outstanding as at 31 December, 2014*
$18.93 - $44.99	105,685
$45.00 - $48.74	109,930
$49.62 – $77.31	84,724
$79.32 - $96.87	95,775
Outstanding at 31 December, 2014	396,114

Notes to the financial statements

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23. Share-based payments (continued)

Stock options (continued)

The parent undertaking uses the Black-Scholes valuation model to estimate the fair value of stock options at the grant date. The parent undertaking validates its estimates and assumptions through consultations with independent third parties having relevant expertise. The fair value of each option granted under the Stock Option Plans during 2014 and 2013 was estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions for 2014 and 2013:

	2014	*2013*
Dividend yield (%)	nil	Nil
Expected share price volatility (%)	50.86	46.20
Risk-free interest rate (%)	1.77	1.25
Expected term of option (years)	5.47	5.81

The weighted-average valuation assumptions were determined as follows:

- *Expected stock price volatility:* Options to purchase the Company's stock with remaining terms of greater than one year are regularly in the market. Expected stock price volatility is calculated using the trailing one month average of daily implied volatilities prior to grant date.
- *Risk-free interest rate*: The parent undertaking bases the risk-free interest rate payable on US Treasury securities in effect at the time of grant for a period that is commensurate with the assumed expected option term.
- *Expected term of options:* The expected term of options represents the period of time options are expected to be outstanding. The parent undertaking uses historical data to estimate employee exercise and post-vest termination behaviour. The parent undertaking believes that all groups of employees exhibit similar exercise and post-vest termination behaviour and therefore does not stratify employees into multiple groups in determining the expected term of options.
- *Dividend yield:* The estimate for annual dividend yield is nil because the parent undertaking has not historically paid, and does not intend for the foreseeable future to pay, a dividend

Restricted share awards

The parent undertaking awards equity settled restricted shares to company employees at the discretion of the compensation committee, managed by the ultimate parent. These shares vest on an annual basis over a period of 4 years. Restricted share awards are valued at the daily average of the high and low market price ruling at the date of grant.

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23. Share-based payments (continued)

Restricted share awards (continued)

The following table illustrates the restricted share activity of the company during 2013 and 2014:

	2014	*2013*
	No.	*No.*
Outstanding as at 1 January, 2014	101,308	107,891
Granted during the year	95,154	68,806
Cancelled during the year	(11,137)	(46,413)
Vested	(32,489)	(28,976)
Transfer in due to business acquisition	12,127	-
Outstanding & unvested at 31 December 2014	164,963	101,308

The weighted average fair value of restricted share awards granted to company employees during the year was US$92.78 (2013 – US$66.00).

Performance accelerated restricted shares (PARS)

The parent undertaking awards equity settled PARS to eligible members of the global Senior Management team based in the UK. These shares are awarded at the discretion of the compensation committee, managed by the ultimate parent. The vesting of these shares occurs as key performance indicators relating to clinical and commercial milestones are achieved.

Performance accelerated restricted shares are valued at the daily average of the high and low market price ruling at the date of grant.

The following table illustrates the PARS stock activity of the company during 2014 and 2013:

	2014	*2013*
	No.	*No.*
Outstanding as at 1 January	7,312	4,500
Granted during the year	29,375	5,625
Vested	(2,500)	(2,813)
Outstanding & unvested at 31 December	34,187	7,312

The weighted average fair value per share of PARS share awards granted to company employees during the year was US$105.82 (2013 – US$45.11).

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at 31 December 2014

23. Share-based payments (continued)

Performance accelerated restricted shares (PARS) (continued)

The total expense recognised for share-based payments in respect of employee services received during the year to 31 December 2014 is £5,065,811 (2013 – £3,561,163). The expense is split between each scheme as follows:

	2014	*2013*
	£'000	*£'000*
ESPP Employee share purchase plan	234	172
Stock options	2,441	1,940
Restricted share awards	42	1,321
PARS Performance accelerated restricted shares	2,349	128
	5,066	3,561

24. Related party transactions

The company has not disclosed details of transactions with other wholly owned Vertex Pharmaceuticals Incorporated group companies as allowed by the exemption in paragraph 3(c) of FRS 8. No other related party transactions have been entered into.

25. Subsequent events

The company entered into a new lease for an office in London during the first quarter of 2015. This office will be the new headquarters of the non-North American Vertex operations. The funding requirements are being met by the Parent undertaking.

On 4 June, 2015, the Vertex Group entered into a strategic collaboration and license agreement (the "Parion Agreement") with Parion Sciences, Inc. ("Parion"). Pursuant to the agreement, the Company is collaborating with Parion to develop investigational epithelial sodium channel ("ENaC") inhibitors, including VX-371 (formerly P-1037) and P-1055, for the potential treatment of cystic fibrosis, or CF, and other pulmonary diseases. VPEL made an up-front payment of $48million.

In the third quarter of 2015 VPEL acquired the wholesale distribution licences for export markets where the Vertex group does not have a limited risk distributor (LRD) or the LRD does not have the appropriate licence. During 2015, further LRD's in Austria, Portugal, Sweden & Switzerland were established as subsidiaries of VPEL.

On 26 October, 2015, the Company entered into a strategic collaboration, option and license agreement (the "CRISPR Agreement") with CRISPR Therapeutics AG and its affiliates ("CRISPR") to collaborate on the discovery and development of potential new treatments aimed at the underlying genetic causes of human diseases using CRISPR-Cas9 gene editing technology. The Company has the exclusive right to license up to six CRISPR-Cas9-based targets. In connection with the CRISPR Agreement, the Company made an upfront payment to CRISPR of $75.0 million and will make a $30.0 million investment in CRISPR pursuant to a convertible loan agreement.

Notes to the financial statements

at 31 December 2014

26. Ultimate parent undertaking and controlling party

The directors consider the ultimate parent undertaking and controlling party to be Vertex Pharmaceuticals Incorporated, a company incorporated in the United States of America. This entity heads the smallest and largest group in which the results of the company are consolidated. The immediate parent from 1 January 2014 to 30 November 2014 was Vertex Pharmaceuticals Incorporated. From 1 December 2014 the immediate parent was Vertex Pharmaceuticals (Cayman) Limited. Copies of the parent's group financial statements may be obtained from The Secretary, Vertex Pharmaceuticals Incorporated, 50 Northern Avenue, Boston, Massachusetts, USA.