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Technical Director
File Reference No. 2020-500
FASB
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Subject: File No. 2020-500 Invitation to Comment, *Concepts Statement No. 8, Conceptual Framework for Financial Reporting – Chapter 4: Elements of Financial Statements*

Dear Technical Director:

Pfizer Inc. is a research-based, global biopharmaceutical company headquartered in New York. We discover, develop, manufacture and market leading medicines and vaccines. In 2019, we reported revenues of $51.8 billion, pre-tax income from continuing operations of $17.7 billion and total assets of $167.5 billion.

Pfizer supports the Board's efforts to improve the elements of financial statements, which is a critical component of the conceptual framework. We recognize that most of the proposed chapter comes from *Concept Statement No. 6, Elements of Financial Statements ('CON 6')*, with changes intended to clarify and improve upon previous elements. We do not disagree with many of the concepts discussed by the Board in this invitation to comment, but we believe some changes may create confusion and diversity in practice. While we understand that the Board is trying to separate the matters of recognition, measurement, and display from the definitions of the elements of financial statements in the Board's conceptual framework project, we believe many of these matters are so interrelated that the proposed changes reduce the usefulness of the elements definitions.

General

Overall, we believe that it may be helpful for preparers to better evaluate the proposed changes if the Board provided additional clarity on the overall purpose of this project. Currently, we believe that there is some confusion among preparers as to whether these proposed changes are meant to change the current population of assets and liabilities, and the classification of items between revenue, expenses, gains and losses. In some cases where there is no authoritative other guidance, preparers currently rely on the existing definitions in CON 6 as the basis for accounting assessments. We have provided some examples in our discussion below. We believe the existing conceptual definitions are well understood by both preparers and financial statement users, and we would have concerns that the proposed changes could significantly impact existing accounting, create diversity in practice, and increase cost and complexity.

Assets

The existing definition of an asset under CON 6 states "Assets are probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events." The proposed new definition in CON 8 would be "An asset is a present right of an entity to an economic benefit."

Removal of Probable

We believe the elimination of the term "probable" (i.e. "likely to occur") from the proposed conceptual definition of an asset could have unintended consequences as more transactions may qualify as an asset. This would also increase the complexity and cost of financial reporting relative to current practice. In the pharmaceutical industry, we enter into agreements to research, develop, manufacture and commercialize potential products through collaboration agreements. These collaboration agreements are governed by a signed contract which gives us the exclusive right to use, research, develop, manufacture, commercialize, and otherwise exploit pharmaceutical compounds. The collaboration arrangements could have a variety of terms and may include our receiving rights to the compound in exchange for our services, upfront payments, milestone payments, future profit sharing, etc. We often receive these rights to a medical compound while the compound is still in the research and development stage prior to regulatory approval and prior to evidence that it is a commercially viable product. The rights we receive could be interpreted as meeting the proposed definition of an asset (i.e., a present right of an entity to an economic benefit), regardless of whether or not it is probable that the compound will result in an approved product. Similarly, upfront payments, milestone payments and in-license agreements during ongoing research and development could be interpreted as meeting the definition of an asset prior to having a commercially viable product, as elimination of the word probable could be interpreted as removing a required threshold of certainty for the future economic benefit.

Another example of potential implications in the pharmaceutical industry is that we sometimes manufacture inventory "at risk" prior to obtaining regulatory approval for commercial sale, and prior to launching commercial sales. Since the compound itself is still subject to ongoing research and development, and regulatory review and approval, we make judgments as to the point in time at which the pre-approval, or pre-launch, inventory should be expensed or capitalized. Since there is no accounting standard that specifically addresses this fact pattern, we use the current definition of "…probable future economic benefit…" to aid in making this accounting determination. Removing the word probable from the accounting definition of an asset would make the decision more difficult and likely create diversity in practice.

Accounting Standards Codification ("ASC") 730 requires research and development costs to be expensed as incurred, except that assets purchased for use in research and development should be capitalized if they have an alternative future use. In addition to the "alternative future use" criteria, the purchased asset must also meet the definition of an asset. This standard is well understood by preparers and users of financial statements. International Accounting Standards ("IAS") 38 however distinguishes between research and development costs. Per IAS 38 research costs must be expensed as incurred and development costs must be capitalized when certain criteria are met. The new definition of an asset may be interpreted to have a lower threshold for capitalizing an asset, and may cause confusion as to whether it is the intention of the Board for companies to ultimately begin capitalizing the intangible asset value of development efforts, similar to IAS guidelines.

Removal of "Control"
We understand the Board's view on how control is interrelated to the proposed definition of an asset. However, we believe that the concept of control is so fundamental to many key accounting standards and the application of the definition itself that the explicit term "control" should be included in the conceptual definition of an asset. For example, ASC 606 Revenue from Contracts with Customers notes "The Board's description of control is based on the meaning of control in the definition of an asset in the Board's respective conceptual framework. Thus, the Board's determined that control of a promised good or service (that is, an asset) is the customer's ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. (ASU 2014-09, BC.120). Additionally, we believe the Board is of the opinion that in order to have a present right, one must have control. In BC4.16 of the proposed chapter, the Board states, "… control references the existing right that has the ability to generate economic benefits, or potential economic benefits, and to restrict others access to those benefits." In an accounting analysis of whether a preparer has a present right, we believe an assessment of the indicators of control would be a primary resource that will be utilized; accordingly, it would be helpful to explicitly include the term "control" in the conceptual definition. Lastly, we believe that the concept of control is also essential in determining when to derecognize an asset. For all of these reasons, we would encourage the Board to reconsider the asset definition as currently presented.

Other Considerations
Also, we question whether the Board believes that the change in asset definition may influence current or future standard-setting projects in this area, such as the business combination project. We would encourage the Board to expand its discussion of business combinations and how the change in the definition of an asset impacts the asset vs. business combination project.

Liabilities
The existing definition of a liability under CON 6 states "Liabilities are probable future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events" The proposed new definition in CON 8 would be "A liability

is a present obligation of an entity to transfer an economic benefit."

Removal of Probable
We believe the elimination of the term "probable future sacrifices" from the proposed conceptual definition of a liability may have unintended consequences. For example, under the current conceptual framework, a contingent liability would be recognized for ongoing litigation if a loss is probable and estimable. Under the proposed conceptual definition, probable has been removed from the definition and we believe it is unclear how ongoing litigation or other claims for which the outcome is still uncertain but for which a loss is considered probable would meet the definition of a liability. Since the litigation or other types of claims in this fact pattern has not yet been resolved, it doesn't seem as though they would meet the definition of a liability (i.e. "a present obligation") until resolution has been settled. We appreciate the Boards efforts to clarify the distinction between the existence and measurement of a contingent liability in paragraph E64, but we do not believe the proposed definition is clear in defining when a recognized liability exists in certain cases.

Conversely, we believe certain transactions that did not meet the definition of a liability in CON 6 will qualify as liabilities under the definition of a liability in this proposed chapter. For example, in the pharmaceutical industry we enter into collaboration arrangements where we may agree to make milestone payments, contingent on the achievement of key milestones in the development and commercialization of an asset. Under the current conceptual framework, we do not recognize a liability simply because a contractual promise to make a milestone payment exists. However, under the proposed conceptual definition of a liability, these contractual agreements could be interpreted as meeting the definition of a liability (i.e. a present obligation of an entity to transfer an economic benefit), regardless of whether it is or is not probable that the underlying asset will reach the milestone. This would also increase cost and complexity associated with how to value these liabilities.

Transfer of Assets or Shares
We support the Board's decision to allow an obligation to transfer either assets or, in certain limited circumstances, an entity's own shares to meet the definition of a liability. We encourage the Board to provide clarity on their intent of the proposed definition and whether there are broader implications on shared based compensation or debt vs. equity.

Revenue, Expenses, Gains and Losses
The elimination of the terminology "ongoing major or central operations" from the definition of Revenues and Expenses, and the elimination of the terminology "peripheral or incidental transactions" from the definition of Gains and Losses, makes the distinction between revenue and gains, and expenses and losses less clear and less useful. We believe the eliminated words are well understood by preparers and users, and represent key differentiators between the elements and could impact the classification of certain transactions, including upfront and pre-approval milestone payments earned from our collaboration partners when our performance obligations

include providing R&D services, royalty payments received from our collaboration partners and gains/losses on sales on fixed assets. Additionally, the definition of a customer in Topic 606 refers to an entity's 'ordinary activities' with the notion of ordinary activities being derived from the definitions of revenue in the CON 6l framework (ASU 2014-09, BC.53). We recommend that the presentation elements stay within the definition.

Additionally, we would encourage the Board to clarify paragraph E91, which says that "gains and losses in similar amounts would not be expected to reoccur frequently or at all." In the pharmaceutical industry, collaboration arrangements are common, often recur each reporting period and often are presented in gains and/or losses, rather than revenue. For example, when our performance obligations included providing R&D services to our collaboration partners, we recognize milestone payments earned over the development period for the collaboration products. We may also sell rights to internally developed in-process research and development or internally generated developed technology, in return for payments on future sales, if any, from the purchaser. The company concludes that the transferred asset is not a business. For example, we may enter into multi-year arrangements with other companies entitling us to royalty income which are generally presented as gains, rather than revenue. The royalty income earned may be consistent year after year resulting in the recognition of gains, for similar amounts, on a regular basis for an extended period of time. There is a risk that companies may interpret the guidance to mean that income from similar type of arrangements should be classified as revenue due to the frequency of the transaction and the elimination of "ongoing major or central operations" in the revenues definition. We believe there are also other examples of gains and losses that reoccur frequently and are included on gains and losses, such as income from equity investments, increases or decreases in the fair value of publicly traded equity securities, etc.

We appreciate the Board's solicitation of input and the opportunity to provide feedback on the Invitation to Comment and would be pleased to discuss our perspectives on these issues with you at any time.

Very Truly Yours,

Jennifer B. Damico

Jennifer B. Damico
Senior Vice President and Controller

cc: Frank A. D'Amelio
Chief Financial Officer and Executive Vice President, Global Supply