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November 19, 2020

Hillary H. Salo
Technical Director
Financial Accounting Standards Board
401 Merritt 7, P.O. Box 5116
Norwalk, CT 06856-5116

Re: File Reference No. 2020-500

Dear Ms. Salo:

Eli Lilly and Company ("Lilly") appreciates the opportunity to comment on the Financial Accounting Standards Board's ("FASB's") Proposed Statement of Financial Accounting Concepts, *Concepts Statement No. 8, Conceptual Framework for Financial Reporting – Chapter 4: Elements of Financial Statements* (the "proposed Concepts Statement"). Lilly is a publicly traded multinational pharmaceutical company with global operations.

Lilly welcomes the efforts of the FASB to develop an improved conceptual framework, specifically as pertains to Elements of Financial Statements ("Elements"). Acknowledging that the intent of these efforts is to solidify the foundation for developing future accounting standards, we feel certain of the changes proposed will have the opposite effect on existing accounting standards that do not otherwise have more prescriptive guidance. Further, as Lilly has not observed inconsistencies with the current Elements definitions found in *Statement of Financial Concepts No. 6 – Elements of Financial Statements (As Amended)* ("CON 6"), we strongly recommend retaining certain key wording from CON 6 in the proposed Concepts Statement, including:

- **"Control"** – definition of an asset
- **"Probable"** – definition of both an asset and a liability

We further strongly recommend no change to the existing CON 6 definitions of Revenue, Expenses, Gains and Losses.

Further explanation as to our position on these matters follows.

ASSETS

We feel that there are key terms from the current definitions of assets in CON6 that, if removed in the proposed Concepts Statement, will result in added complexity in determining what is (or is not) an asset, as well as increasing the population of assets to include that may have a very low probability of future economic benefit. This could, in turn, result in an increase in impairment losses in future periods, adding needless volatility to the financial results and causing unnecessary distortion across reporting periods. As a result, registrants will likely non-GAAP these items as they may materially distort the underlying results of operations.

The current definition of an asset in CON 6 states "(a)ssets are probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events," where the term "probable" is further noted in Characteristics of Assets in CON 6 as "intended to acknowledge that business and other economic activities occur in an environment characterized by uncertainty in which few outcomes are certain."

The proposed Concepts Statement's definition of an asset (a) removes "probable," and (b) changes "future economic benefits obtained or controlled" to be "present right to an economic benefit." We feel both of these changes would not accomplish the intent of making the existing CON 6 definition of an asset more understandable and more consistent in application across GAAP.

- ***Removal of "probable"*** – The proposed Concept Statement's Basis for Conclusions BC4.10 implies that removing "probable" eliminates risk of the asset definition not being met as a result of a low probability threshold for future economic benefit. We counter that probability is a very necessary feature in the definition of an asset, and is harmonious across GAAP where probability is a pervasive and ingrained feature throughout many FASB Topics (including the recent and substantive *Topic 606 – Revenue* and *Topic 842 – Leases*). Additionally, as it pertains to assets, probability is used prevalently in the pharmaceutical industry, including for pre-launch inventory for a drug that has not yet received regulatory approval. In this industry usage, probability aligns with the technical meaning of "probable" that is found in the FASB Master Glossary. Without "probable," it is implied that companies must instead consider what is possible when considering whether an asset has an economic benefit, thus increasing the population of items to be considered assets, as well as adding significant and unnecessary complexity to the financial reporting requirements.

  The use of "probable" is also a key characteristic used by companies in determining the definition of assets acquired to be used in research and development activities, also known as IPR&D assets. The original 2001 AICPA Practice Aid *Assets Acquired in a Business Combination to be used in Research and Development Activities* ("2001 Practice Aid"), developed by the AICPA Staff and IPR&D Task Force, incorporated a definition of an asset that closely mirrored that which is found in CON 6, noting that one characteristic of an asset is that "it embodies a probable future economic benefit…to contribute directly or indirectly to future net cash inflows." The 2013 AICPA Accounting & Valuation Guide *Assets Acquired to Be Used in Research and Development Activities* ("2013 Accounting & Valuation Guide") which superseded the 2001 Practice Aid removed this language and instead noted in §2.06, §3.02 and §3.14 (via footnote 2) that such acquired assets must meet the definition of an asset in CON 6 (which includes "probable" in its definition). While we acknowledge the AICPA guidance is nonauthoritative, it is a primary reference source utilized by both financial statement preparers and the reviewers and auditors of those financial statements in lieu of absent authoritative guidance. As such, there is consistency in the application of the AICPA IPR&D guidance, and the removal of "probable" in the definition of an asset would result in an increase of the population of such acquired assets on the statement of financial position, for the same reasons and with the same concerns as noted in the preceding paragraph.

We strongly recommend that the FASB not remove "probable" from the definition of an asset.

- ***Removal of "control"*** – The proposed Concepts Statement removes "control" from the primary definition of an asset. We acknowledge the proposed Concepts Statement's terminology "present right to an economic benefit" in the primary definition of an asset is elucidated in the Characteristics of Assets subsection, which states these characteristics, when combined, "control others' access to the benefit." However, we see removing "control" from the primary definition to be detrimental.

  Similar to the concept of "probability," the concept of "control" is one that is pervasive and ingrained throughout many FASB Topics (including the recent and substantive *Topic 606 – Revenue* and *Topic 842 – Leases*). By removing it, there is unnecessary subjectivity introduced to the determination of what should be considered an asset. While we acknowledge that BC4.12 states that the new definition "maintain(s) the notion of control," we counter that the FASB must then recognize that specifically removing this definition in favor of a "notion of control" introduces ambiguity to the definition of an asset which currently requires control, and its removal is tantamount to inconsistency in the application of the definition of what is or is not an asset. We note Ms. Christine A. Botosan's viewpoints against removal of "control" in BC4.42 through BC4.46 and fully align with them and urge the Board strongly consider those opinions equal to those of our own.

  We strongly recommend that the FASB not remove "control" from the definition of an asset.

LIABILITIES

The current definition of a liability in CON 6 states "(l)iabilities 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," where the term 'probable" is further noted in Characteristics of Assets in CON 6 as "intended to acknowledge that business and other economic activities occur in an environment characterized by uncertainty in which few outcomes are certain."

The proposed Concepts Statement's definition of a liability removes "probable," and for many of the same reasons discussed in the ASSETS section above, we feel that removal of the key term "probable" from the current definition of liabilities will result in added complexity in determining what is (or is not) a liability, as well as increasing the population of liabilities to include those with a very low probability of future sacrifice of economic benefits.

Specifically, we note that for companies in the pharmaceutical industry, agreements with early-stage development laboratories to in-license unproven molecules almost always include development milestones and approval milestones. Under the proposed definition of a liability that excludes "probable," a company in-licensing a molecule may therefore accelerate the recording of certain milestone payments as a liability on its statement of financial position with an offset to expense on the statement of operations. In turn, an inverse probability of having to reverse the liability (and expense) in future periods results, adding needless volatility to the financial results of the in-licensing company and causing unnecessary distortion across reporting periods.

Additionally, we request that the Concept Statement address the disconnect between the definition of a liability and the accounting for loss contingencies. Specifically, there should be discussion added that defines loss contingencies directly as a type of contingent liability, as FAS 5 (now ASC 450-20) predates CON 6 and there is otherwise no authoritative guidance pertaining to how or whether loss contingencies meet the definition of a liability. Please refer to the comment letter provided by the Financial Executives International's (FEI) Committee on Corporate Reporting (CCR), of which Eli Lilly and Company is a member, for an example that exemplifies the issue.

We strongly recommend that the FASB not remove "probable" from the definition of a liability.

REVENUE, EXPENSES, GAINS AND LOSSES

We strongly oppose the suggested changes to the CON 6 definitions of Revenue, Expenses, Gains and Losses which, in our opinion, are well understood and clearly defined.

Of significant importance is the proposed Concept Statement's removal of the qualifying statement from CON 6 that revenues and expenses source from "activities that constitute the entity's ongoing major or central operations." The proposed Concept Statement also removes the Characteristics of Revenues section from CON 6 which reemphasized that revenue and expenses are tied with an entity's ongoing major or central operations. Removal of this qualifying language, coupled with the narrow guidance provided for in the proposed Concept Statement which states that gains and losses will typically result from four circumstances, would arguably lead to confusion as to how certain other activities will be recorded. Considering the abundance of effort in preparing *Topic 606 - Revenue*, we agree with the comments of Ms. Botosan in BC4.54 that having a different definition of revenue in a Concept Statement from that which is in *Topic 606 - Revenue* is less than ideal, and that the proposed definitions do not enhance the usefulness of the Conceptual Framework.

Further, note the following items that may now be required to be reported significantly differently under the Proposed Concepts Statement:

> Investment income – *currently recorded as a gain for companies whose primary operations are not treasury/banking/investment/brokerage related – proposed Concepts Statement (BC4.38) indicates this should be recorded as revenue*
>
> Sublease income – *some companies may net sublease income against the related head lease expense, while others may report sublease income as a separate line item within the same category as the head lease expense. Proposed Concepts Statement implies this income should be recorded as revenue, absent other authoritative guidance.*
>
> Adjustments to allowance for credit losses – *some companies record as an expense – proposed Concepts Statement (E89b) suggests this should be recorded as gain/loss absent other authoritative guidance*
>
> Impairments of operating assets – *some companies record as an expense – proposed Concepts Statement (E89b & E91) suggests this should be recorded as a loss absent other authoritative guidance*

We strongly oppose any change to the current definitions of Revenue, Expenses, Gains and Losses.

We again note that the objective the FASB noted for this project is "providing a foundation for future standards." As existing standards are far more prevalent, significant and essential to financial reporting, we urge that the objective must consider the impact of the project on existing standards (acknowledging overriding guidance that may exist in those standards) and strive to align with the guidance in those standards. Changing the fundamental bases for definitions of assets, liabilities, revenue, expenses, gains and losses would have the opposite effect of that which is intended, which should be to provide useful and understandable information to users of financial statements.

We thus reaffirm our recommendation to not remove certain key descriptors (e.g. "probable," "control") from the CON 6 the definitions of assets and liabilities, and to not change any of the wording from the CON 6 definitions of revenues, expenses, gains and losses.

We appreciate the opportunity to express our view and concerns regarding the proposed accounting standards update. If you have any questions regarding our response, or would like to discuss our comments further, please call me at (317) 651-2310.

Sincerely,

ELI LILLY AND COMPANY

/s/Donald A. Zakrowski

Donald A. Zakrowski
Vice President, Finance and Chief Accounting Officer