Merck & Co., Inc.
One Merck Drive
P.O. Box 100
Whitehouse Station, NJ 08889-0100

MERCK

October 28, 2005

Letter of Comment No: 67
File Reference: 1204-001

Technical Director
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856-5116

Re: File Reference No. 1204-001

Dear Director:

Merck & Co., Inc. is a New Jersey based corporation with its principal place of business at One Merck Drive, P.O. Box 100, Whitehouse Station, New Jersey 08889-0100. The Company is a global research-driven pharmaceutical products organization that discovers, develops, manufactures and markets a broad range of innovative products to improve human and animal health. We are pleased to provide you with our comments on the Exposure Draft "Business Combinations, a replacement of FASB Statement No. 141".

Although we support the Financial Accounting Standard Board's effort to promote international convergence and to improve financial reporting, we have conceptual concerns about several of the proposals under the exposure draft. If adopted, the proposed accounting may cause less predictable and more volatile short-term earnings as well as require significant fair value assessments by management. Specifically, the areas of most concern include the inconsistencies created by capitalizing in-process research and developments (IPR&D) costs, accruing contingent consideration at fair value on the date of acquisition and expensing acquisition-related costs.

To better understand the research and development process for pharmaceutical companies, consider the following stages of product development and probabilities of success (POS) of research and development activities as product candidates proceed from basic research though product launch.

Research and Development Process

Basic Research*	Pre-Clinical	Phase I	Phase IIa	Phase IIb	Phase III	Product Launch
Identify rational disease targets, and then discover and develop drug candidates which affect the target in a desired manner	Synthesize compound to begin animal testing required by the FDA	First administration of new drug candidate to humans	Shift emphasis from healthy patients in Phase I to targeted disease	Large scale studies – define optimal doses and confirm efficacy and safety in patients	Large scale studies – define optimal doses and confirm efficacy and safety in patients	Product reaches technical success, but does not guarantee commercial success
< 10%	*15%*	*20%*	*25%*	*60%*	*80%*	

Approximate POS - industry averages

* According to the Tufts Center for the study of Drug Development database, out of every 3,000-10,000 compounds identified in the basic research phase, only one is successfully introduced as a viable commercial product in the marketplace.

Under current accounting, in accordance with FASB Statement No. 2, *Accounting for Research and Development Costs*, and FASB Interpretation No. 4, *Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method*, costs allocated to identifiable assets acquired as part of a business combination to be used in research and development activities with no alternative future use should be charged to expense as incurred, similar to internal research. In order for a project to be expensed immediately as acquired research, the project must be identifiable and its fair value must be able to be estimated with reasonable reliability. Upon identifying a compound as a lead drug candidate in the basic research phase, a specific project must have commenced. However, it is not until the pre-clinical phase that enough information is available to determine its fair value.

In-Process Research and Development (IPR&D)

Under the proposed Statement, tangible and intangible assets used in research and development acquired in a business combination with no alternative future use should be recognized and measured at their acquisition-date fair values. While we understand the logic behind recording IPR&D at a risk-adjusted fair value, using a range of possible outcomes with different probabilities, there are clear inconsistencies with current accounting for research and development costs. Internally developed research and development as well as assets licensed or acquired outside a business combination that are to be used in a particular research and development activity (such as license deals or asset purchases) are expensed as incurred in connection with FASB Statement No. 2 and Interpretation No. 4. In addition, Interpretation No. 4 explicitly states, and we firmly agree, that consistency is appropriate when accounting for research and development costs. Excerpts from Interpretation No. 4 are as follows: "costs assigned to assets to be used in a particular research and development project and that have no alternative future use shall be charged to expense at the date of combination. Therefore, the accounting for the cost of an item to be used in research and development activities is the same under paragraphs 11 and 12 of Statement No. 2, whether the item is purchased singly, or as part of a group of assets, or as part of an entire enterprise in a business combination accounted for by the purchase method."

Furthermore, we are concerned that capitalizing IPR&D as an indefinite-lived intangible asset would require significant judgment when testing for impairment each year, as many research and development projects may have alternative uses in the future. Therefore, the timing and valuation of potential impairments will be highly subjective, and determining whether or not an R&D

project is impaired may be expensive as multiple internal company resources would be involved (research groups including clinical, drug metabolism, pharmaceutical R&D, safety assessment and other corporate groups).

Lastly, we are concerned about investor confusion regarding the capitalization of IPR&D. Since the pharmaceutical industry is R&D intensive, it's anticipated that companies would need to disclose in the footnotes or MD&A which IPR&D capitalized assets would have a low probability of success and the potential for future write-offs. Investors may be uncertain as to why these assets are included in the Company's balance sheet as viable assets but then accompanied by disclosure that there is a high probability that these assets may be written off in the future.

Contingent Consideration

The proposed Statement would require all items of consideration transferred by the acquirer to be measured and recognized at fair value at the acquisition date, including contingent consideration. In the pharmaceutical industry, contingent payments are directly associated with the continued success of the products being acquired throughout the development process and are a mechanism for sharing risk with the counterparty. Contingent payments are highly subjective in nature, take years to determine and may be significant to the transaction.

The determination of contingent payments includes risks associated with intellectual property, developmental and regulatory hurdles and commercial viability. By their nature, these contingencies often do not lend themselves to observable market values as they are not frequently exchanged or sold. As a result, the fair value assigned to contingencies may not be accurate, since the amount recognized is not likely to be the amount ultimately settled or realized. This highly subjective fair value computation will result in an inconsistent application across the pharmaceutical industry. Moreover, there is likely to be much concern regarding the difficulty in auditing the probabilities assigned to some of the most subjective values in the acquisition.

The proposed Statement requires all changes in fair value of the liability subsequent to the date of acquisition to be recognized in income during the period incurred. Our concern is that accretion of the liability each reporting period may lead to significant income statement volatility primarily as a result of changes in product candidates' probability of success as they proceed from pre-clinical trials through Phase III. Furthermore, upon product candidate failure, immediate income recognition would occur, which leads to paradoxical accounting (e.g. adverse business results lead to a favorable accounting impact).

Under the proposed Statement, the model for recording contingent payments is inconsistent with the recognition of IPR&D costs in a business combination. Although we have expressed our concerns about recording IPR&D as an asset, if adopted, contingent consideration should be consistently applied. Under the proposed model, we agree that the fair value of the liability should be determined based on the compounds probability of success. However, to better represent the economics of the transaction and the matching principle, the Board should consider a model in which contingent payments are capitalized as an amortizable asset and amortized only after FDA approval has occurred and they are commercially viable products. This way, it eliminates income statement volatility for products which fail because the accrual would be reversed against the amortizable asset. Furthermore, under a success outcome, the expense recognition associated with contingent payments are matched with product sales. The cumulative expense under this method would be identical to the expense recognition under the proposed Statement, only the timing of expense is different.

To illustrate the alternative approach, consider the following example of an acquisition made in 2004, including contingent milestone payments beginning in 2006, in which the pre-launch product fails in the first quarter of 2007. The example compares (1) current accounting, (2) the proposed accounting under the exposure draft and (3) an alternative accounting approach (as described above):

Acquisition with Contingent Consideration

(Assume acquisition in 2004 and pre-launch product failure in first quarter of 2007)

Scenario	2004	2005	2006	2007	Cumulative Expense
Current Accounting (1)					
Purchase Price Adjustment	-	-	35	-	-
Amortizable Asset	-	-	-	-	-
IPR&D Expense (4)	106	-	-	-	**106**
Total Expense	106	-	35	-	**106**
Proposed Accounting (2)					
Expense	16	12	50	-	**78**
Accrual Reversal to Income	-	-	-	(121)	**(121)**
Amortizable Asset	-	-	-	-	**-**
IPR&D Write-off (4)	-	-	-	184	**184**
Total Expense	16	12	50	63	**141**
Alternative Accounting (3)					
Expense	-	-	-	-	**-**
Accrual Reversal to Income	-	-	-	(121)	**(121)**
Amortizable Asset	-	-	-	78	**78**
IPR&D Write-off (4)	-	-	-	184	**184**
Total Expense	0	0	0	141	**141**

(1) In accordance with FASB Statement No. 2 and FASB Interpretation No. 4, IPR&D is expensed at the date of acquisition. Assume in 2006 the contingency was met and the first milestone payment of $35 million was made resulting in a purchase price adjustment.

(2) Under the proposed accounting, assume a $78 million accrual was recorded at fair value for contingent milestone payments at the date of acquisition and accreted to fair value from 2004-2006. Upon product failure in 2007, the fair value of the accrued contingent consideration would be reversed to income and the IPR&D asset reversed to expense.

(3) Under the alternative approach, the accretion related to the accrued liability would be recorded as an intangible asset during 2004-2006. Upon product failure in 2007, the fair value of the contingent liability would be reversed to income and the IPR&D asset and amortizable asset to expense.

(4) IPR&D (existing GAAP)	$106
Contingent Consideration	78
IPR&D (proposed GAAP)	$184

The alternative model would better align the accounting for contingent consideration for business combinations with the current accounting treatment for licensing transactions and asset purchases. Under those current accounting models, contingent payments are capitalized and amortized only after receiving regulatory approval, if required.

Acquisition-Related Costs

Under the proposed Statement, acquisition-related costs are not considered part of the business combination, and generally, would be expensed in the period that the related services are received. We disagree with this view and consider acquisition-related costs (e.g. investment banking fees, legal and accounting fees related to the business combination) directly related to the transaction and should be considered part of the fair value exchange between the acquirer and acquiree. These costs would not have been incurred if it was not for the business combination.

Thank you for the opportunity to provide comments on the proposed exposure draft. We would be pleased to discuss our views with you at your convenience.

Sincerely,

/s/ Richard C. Henriques

Richard C. Henriques
Vice President, Controller
Merck & Co., Inc.

cc: J.C. Lewent - Executive Vice President & Chief Financial Officer