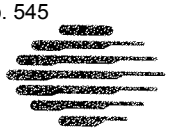
ALLERGAN

2525 Dupont Drive, P.O. Box 19534, Irvine, California, USA 92623-9534 Telephone: (714) 246-4500 Website: www.allergan.com



VIA EMAIL

October 22, 2010

Technical Director
File Reference No. 1820-100
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

Re: Exposure Draft—Proposed Accounting Standards Update, Revenue Recognition (Topic 605): Revenue from Contracts with Customers

Dear Technical Director:

Allergan, Inc., a Delaware corporation ("Allergan"), appreciates the opportunity to respond to the Financial Accounting Standards Board (the "Board") regarding the Exposure Draft, Proposed Accounting Standards Update, Revenue Recognition (Topic 605): Revenue from Contracts with Customers (the "Proposed Update"). Allergan is a publicly traded, multi-specialty health care company listed on the New York Stock Exchange under the symbol "AGN."

We support the Board's effort to consolidate the expansive current revenue recognition guidance and we agree that a principles-based standard is the best approach to codify the spirit of today's accounting rules, but we would ask the Board not to lose sight of the foundational concepts of financial reporting along the way. When we previously wrote the Board indicating our support for a convergence process with International Financial Accounting Standards ("IFRS") prior to potentially adopting IFRS in the United States, we did not envision a conversion to a completely new set of accounting principles as opposed to the convergence of standards already currently in place under either IFRS or GAAP, which have already been tested in the marketplace. As such, we ask the Board to consider suspending deliberations on this Proposed Update and going back to a convergence agenda rather than a conversion agenda. Creating new, untried accounting principles in the sensitive and risky area of revenue recognition is simply not in the best interest of users of financial statements.

We believe that one of the best principles-based accounting statements in the world is Statement of Financial Accounting Concepts No. 5, *Recognition and Measurement in Financial Statements of Business Enterprises* (CON5). Within CON5, one finds multiple, sometimes competing principles that work toward the objective of reliable, accurate financial reporting, namely *Measurability, Relevance, and Reliability.* It is the balance of these principles that enables reliable financial reporting. In order to apply those principles to revenue recognition, CON5 sets out the following required pre-conditions for revenue to be recognized: 1) revenue must be *earned* and 2) revenue must be *realized or realizable.* We believe one of the chief flaws of the

Proposed Update is that it focuses solely on determining when and estimating how much revenue is earned, and removes the requirement for revenue to be realizable. In doing so, both *Measurability* and *Reliability* are compromised and along with them reliable, accurate and useful financial information for investors.

Additionally, we contend that for financial statements to be *Relevant*, they must not only reflect the true economic reality and nature of underlying transactions, but also must be rooted in basic, common sense concepts. If accounting standards require a company to record revenue (and related receivables) that the company believes is more likely than not to never be collected (due to the probability-based measurement principle described in paragraph 35 of the Proposed Update), we don't believe rational financial statement users will have any use for the concept of revenue recognition. Revenue recognition becomes more of a game of chance than of reality (i.e., similar to a Monte Carlo simulation rather than reality). Although a recorded revenue balance might represent the best theoretical, probability-weighted estimate of a potential economic value to be transferred, it will have no *Relevance* to a normal investor who wants to know with reasonable certainty a reliable measurement today of future cash generating potential of a business enterprise. We expect that if the Proposed Update is issued in its current form, the investment community and most other financial statement users would dismiss the relevance of the income statement as a theoretical exercise and turn to the cash flow statement as the only relevant reflection of an enterprise's current economic performance.

We strongly believe that the more accounting standards rely on probability-weighted scenarios and other highly volatile future fair value estimates, the less reliable financial statements become, and the more susceptible they become to manipulation. Imagine the potential volume of audit review comments from inspections by the Public Company Accounting Oversight Board ("PCAOB") using principles prescribed under the Proposed Update that state, "the audit firm failed to obtain 'sufficient competent evidential matter' to perform adequate audit procedures to test a company's probability-weighted estimates of fair value for revenue recognized in its financial statements." Also, the number of estimate iterations required to get a common mean estimate for any fair value is extremely cumbersome and costly if one requires the process to be statistically sound. It takes very little review of recent economic history to know that even the best estimates of future transactions can, and usually do, vary greatly (materially) from actual economic outcomes. We wonder what income statements would have looked like in 2008 and 2009 if the Proposed Update was in effect at that time and probability-based estimates of variable future cash flows moved from a state of "irrational exuberance" to the new paradigm of "great recession." We would surely have heard a chorus of Investor Relations departments explaining to financial statement users that the massive reversals in revenue they were recording had no correlation to current operational profitability. It also requires very little review of accounting fraud cases over the last decade to understand that some companies can and will exploit accounting standards that rely too heavily on management estimates of future economic performance. Imagine what Enron's income statements might have looked like using the principles prescribed in the Propose Update.

For these reasons, we urge the board to retain the critical CON5 concept of "realizable" as it further deliberates the Proposed Update. We believe the relevance of GAAP financial reporting is at stake. **To put it simply: If we abandon CON5, GAAP will not survive.**

As a general comment on principles-based accounting standards, we also note that practical, common-sense exceptions to accounting principles for the purpose of making theoretical principles operational in the real world should not be automatically dismissed as outdated provisions of a bygone, rules-based era. Accounting standards are subject to cost/benefit analyses (as they well should be since the chief users of financial statements are investors who ultimately bear the costs of applying accounting standards) and are applied by accounting departments with finite resources. In order to be effective, principles-based accounting standards must also be practical. As an example of a theoretically pure, but thoroughly impractical accounting principle, we point to the requirement to use a credit risk adjusted interest rate to compute the time value of money in paragraph 45 of the Proposed Standard. No entity outside of the financial institution industry has the internal capability to determine credit risk adjusted interest rates for individual customers. Even then, the internal policies and practices for determining such interest rates will vary between the banks based on evolving risk appetites for various types of transactions and industry concentrations. Although not a theoretically pure application of the concept, we do not believe the integrity of the time-value of money principle would be compromised by the use of a specified prevailing published market interest rate, which is something every entity could apply at minimal cost. We urge the board not to lose sight of the need for practical application of accounting standards as it continues with the agendas of convergence and principles-based standards.

We address the issue-specific questions from the Proposed Update below:

Question 1: Paragraphs 12-19 propose a principle (price interdependence) to help an entity determine whether to:

(a) combine two or more contracts and account for them as a single contract;
(b) segment a single contract and account or it as two or more contracts; and
(c) account for contract modification as a separate contract or as part of the original contract

Do you agree with that principle? If not, what principle would you recommend, and why, for determining whether (a) to combine or segment contracts and (b) to account for a contract modification as a separate contract?

Answer: We agree that if multiple contracts are entered into at or near the same time, or are negotiated as a package with a single commercial objective, there is a high likelihood that they are in substance a single contract and should be accounted for as such. Although we also agree that the price interdependence concept is logical in the context of segmenting a contract, we believe it is more practical to simply apply the multiple performance obligation provisions of the Proposed Update in multiple deliverable contracts rather than create a duplicative paradigm for contract segmentation.

Question 2: The Boards propose that an entity should identify the performance obligations to be accounted for separately on the basis of whether the promised good or service is distinct. Paragraph 23 proposes a principle for determining when a good or service is distinct. Do you agree with that principle? If not, what principle would you specify for identifying separate performance obligations and why?

Answer: We agree that the concept of "distinct" is an appropriate principle for identifying separate performance obligations, but not as currently prescribed in the Proposed Update.

We believe the Par 23(b)(ii) reference to "distinct profit margin" as a condition of a separate performance obligation is inappropriate and opens up the potential for misinterpretation. We understand that the Board used the phrase "distinct profit margin" to convey a combination of "distinct risks" and "distinct resources", but "profit margin" as a concept encompasses more than just these two things. Profit margins are volatile and can change rapidly based on a number of outside influences, such as competition or changes in economic conditions. These issues are unrelated to the nature of the performance obligation. Furthermore, understanding a performance obligation's profit margin implies an ability to readily estimate a theoretical stand-alone selling price, which may or may not be possible. We believe that Par 23(b) should be revised to include three conditions for a good or service to be considered "distinct": (i) goods or services must have a distinct function, (ii) be subject to distinct risks, and (iii) and require separately identifiable resources.

Question 3: Do you think that the proposed guidance in paragraphs 25-31 and related implementation guidance are sufficient for determining when control of a promised good or service has been transferred to a customer? If not, why? What additional guidance would you propose and why?

Answer: We believe the transfer of control guidance is sufficient as currently drafted in the Proposed Update.

Question 4: The Boards propose that if the amount of consideration is variable, an entity should recognize revenue from satisfying a performance obligation only if the transaction price can be reasonably estimated. Paragraph 38 proposes criteria that an entity should meet to be able to reasonably estimate the transaction price.

Do you agree that an entity should recognize revenue on the basis of an estimated transaction price? If so, do you agree with the proposed criteria in paragraph 38? If not, what approach do you suggest for recognizing revenue when the transaction price is variable and why?

Answer: As discussed above, we strongly disagree with the Proposed Update's replacement of "realizable" with "reasonably estimable." We would again refer the Board to its own statements in CON5: "In assessing the prospect that as yet uncompleted transactions will be concluded successfully, a degree of skepticism if often warranted. As a reaction to uncertainty, more stringent requirements have historically been imposed for recognizing revenues and gains as components of earnings than for recognizing expenses and losses."

We note that in *Basis for Conclusions* paragraph 90, the Board "considered whether to constrain revenue recognition if the customer promises a variable amount of consideration," but instead chose to "constrain the transaction price" because, among other reasons, "a significant portion of errors in financial statements have related to the overstatement or premature recognition of revenue." We wonder how the Board expects the Proposed Update to alleviate these issues, when on its face the Proposed Update allows companies to recognize revenues earlier (since they are

no longer required to be realizable) and for amounts that are more likely than not to never be realized (for instance, if a company has solid historical evidence that a specific transaction will result in a certain amount of revenue 40% of the time).

We also note that in *Basis for Conclusions* paragraph 94, one of the reasons the Board rejected an alternative to limit cumulative revenue recognition to amounts that are certain was that "it conflicts with the core principle of the proposed guidance because in some circumstances, an entity would not recognize revenue when a good or service is transferred to the customer." We do not disagree, but we believe that focusing on one "core principle" at the expense of other, more foundational principles leads to nonsensical conclusions. Revenue recognition is complex, and a high quality revenue recognition standard should recognize that there are often competing principles, which must be balanced to yield the best accounting answer. The adherence to one "core principle" at the expense of all other core accounting concepts is the equivalent of building a perfect house on a faulty foundation.

As an illustration of the unnecessary and inappropriate volatility that the Proposed Update would potentially introduce to revenue recognition, please consider the following example from our industry:

> Pharma Company A licenses out an approved technology to Pharma Company B for the exclusive right to sell a product in a specific market for ten years, which is the full estimated economic life of the product through the date of patent expiry. A patent challenge during the licensing term is considered highly unlikely. As consideration for the license transfer, Pharma Company A will receive a 10% royalty on all sales of the product by Company B and will receive a $10 million milestone payment if aggregate Company B sales of the product over the life of the contract exceeds $100 million.
>
> In Year 1 and 2, Pharma Company A recognizes only the royalty revenue received for the period and none of the milestone payment because neither the amount of the future royalty stream or the probability of milestone can be reasonably estimated during these periods.
>
> In Year 3, after two years of sales of in the aggregate of $20 million, Pharma Company A recognizes $8 million of the milestone revenue (ignore discounting for this example) because it believes there is a probability-weighted eighty percent chance Pharma Company B sales will hit the $100 million threshold. Pharma Company A also recognizes $7 million in estimated royalties in Year 3 for all remaining years of the license, since it now has enough history to reasonably project estimated future sales.
>
> In Year 4, a generic pharma company successfully challenges the patent of the licensed product and launches a generic formulation. Pharma Company A determines that there is now zero chance it will receive the milestone, so it reverses the $8 million previously recognized. Future royalties are now determined to be de minimus, so the $7 million of previously recognized future royalties are also reversed.
>
> A summary of revenue recognition and cash flows for this example under both proposed and existing guidance follows:

	Rev Rec Proposed Guidance	Actual Cash Flows	Rev Rec Existing Guidance	Actual Cash Flows
Year 1	0.8	0.8	0.8	0.8
Year 2	1.2	1.2	1.2	1.2
Year 3	**16.5**	**1.5**	1.5	1.5
Year 4	**(14.0)**	**1.0**	1.0	1.0
Year 5-10	0.5	0.5	0.5	0.5
Total	5.0	5.0	5.0	5.0

The volatility in Year 3 and Year 4 relate to the probability-based estimates of variable transaction price that ultimately had no true economic substance. These results reflect the inappropriate volatility that would occur under the Proposed Update that we believe would be confusing and detrimental to financial statement users.

Question 5: Paragraph 43 proposes that the transaction price should reflect the customer's credit risk if its effects on the transaction price can be reasonable estimated. Do you agree that the customer's credit risk should affect how much revenue an entity recognizes when it satisfies a performance obligation rather than whether and entity recognizes revenue? If not, why?

Answer: We do not agree that a customer's credit risk should affect how much revenue an entity recognizes in most circumstances. This is because we do not believe this treatment properly reflects the underlying economics of most transactions. Again, we believe a threshold of "realizable" should be a key factor in determining "whether" an entity recognizes revenue or not. We strongly believe that revenue should not be recognized for an amount that more likely than not will never be realized. Additionally, the majority of entities are not in the business of determining specific degrees of credit risk for customers. We believe that credit risk is viewed by the vast majority of entities as a binary proposition – either a customer is expected to pay in full and therefore is allowed a sale on credit, or is considered a credit risk and sales on credit are limited or sales are only allowed on an upfront payment basis. We believe the complex concept of applying varying degrees of credit worthiness to a portfolio of business implied by the Proposed Update is a practice that does not generally exist outside of the financial institution industry.

We understand why the Board proposed the probability-based credit risk concept in paragraph 43 and agree that in the appropriate context, that concept makes sense. Entities currently record reductions in revenue for similar probability-based estimates of product returns and rebate programs. We believe the Board could retain the benefits of a probability-based credit risk principle and avoid the problematic implications of the provisions currently drafted in the Proposed Update by considering first whether the revenue meets the criteria of realizable, then applying an aggregate method of estimating provisions for credit risk to a population of

realizable revenue transactions, similar to the current methods for estimating and accounting for product returns and rebate programs.

Question 6: Paragraphs 44 and 45 propose that an entity should adjust the amount of promised consideration to reflect the time value of money if the contract includes a material financing component (whether explicit or implicit). Do you agree? If not, why?

Answer: We agree with the concept that long-term receivables should be discounted to reflect the time value of money. However, we strongly believe only receivables that are expected to be outstanding over one year should meet the definition of having a material financing component. Again, from a practical perspective, analyzing the short-term effects of financing arrangements of less than one year is not meaningful and would result in little benefit for the ongoing costs of compliance management. We also object on practical grounds with the provision of paragraph 45 that indicates the discount rate to be used in this calculation should include an element of credit risk. As mentioned above, no entity outside of the financial institution industry is in the business of assigning interest rates to customers based on their credit quality, nor would they have the internal ability to do so without significant additional costs of administration. Therefore, we ask the Board to remove the requirement to use credit risk adjusted interest rates to make the time value of money provision operational.

Question 10: The objective of the Boards' proposed disclosure requirements is to help users of financial statements understand the amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. Do you think the proposed disclosure requirements will meet that objective? If not, why?

Answer: As a general principle, we believe that footnote disclosures should not require the financial statement reader to be an expert in the underlying accounting principles used to record transactions. Rather, the disclosures should communicate the basics of the underlying transactions or balances and provide the reader with a general understanding of the risks and opportunities that result from the use of estimates or professional judgment in accounting for these transactions or balances. The required rollforward of contract assets as currently drafted in the Proposed Update is diametrically opposed to this principle. It is complex, confusing, and very green eyeshade in its presentation format. The rollforward also requires a detailed understanding of the revenue recognition accounting standard for it all to make sense. We believe the bottom line is that investors want to know the net change in reported revenue and any cash flows associated with the contract asset during the period, not necessarily all the ins and outs of various accounting changes in estimates and other categories. We believe the Board should replace the format in the Proposed Update with a more simplified rollforward format that reconciles the beginning and ending balances by summarizing new revenue recognized in advance of cash payments during the period, net changes in prior period contract balance revenue estimates, discount amortization and net cash payments received during the period. Although we do not believe that even the best disclosure format will meet the objective stated above due to the complexity of variable consideration and related probability-weighted based measurement provisions, a simplified rollforward as described above would allow a typical financial statement user to judge potential uncertainty by reviewing overall trends in the more limited "change in estimates" that really matter.

Question 13: Do you agree that an entity should apply the proposed guidance retrospectively (that is, as if the entity had always applied the proposed guidance to all contracts in existence during any reporting periods presented)? If not, why?

Answer: We strongly disagree that the new guidance should be applied retrospectively. Full retrospective application is difficult and costly even when the number of transactions subject to the new guidance is small. But to recompute financial results for every single revenue transaction for a three year period (and likely for many additional years since many contracts in existence three years ago would have initiated in prior years) would require such a huge amount of resources that we doubt most companies would be able to reasonably comply. We remind the Board that companies will not be implementing this guidance in isolation. This Proposed Update is one among many convergence projects that will likely require significant manual resources to implement over the next few years. We believe that none of these requirements can be easily automated.

We believe prospective application in the year of adoption is the best approach. The users of financial statements are fully aware of the new complexity and will surely understand that a reasonable transition period is necessary. A distant second would be to retrospectively apply the guidance to only contracts that were originally initiated in the current and comparative reporting periods presented.

Question 18: Should any of the proposed guidance be different for nonpublic entities (private companies and not-for-profit organizations)? If so, which requirement(s) and why?

Answer: We believe that all for-profit, non-governmental enterprises should account for financial information in the same way, under a single set of high quality accounting standards. We believe allowing for different applications of accounting standards because of company size or public registration on a stock exchange will lead to a confusing proliferation of different accounting treatments for similar transactions, which is contrary to the core concept of comparability of financial statement information. We also believe that if an accounting standard is too complex or too expensive to implement for private companies, it is an strong indicator that the accounting standard does have the appropriate cost/benefit relationship for any company. GAAP should be GAAP. Exceptions should be rare.

Other Issues:

Onerous Contracts: We believe the accounting for onerous contracts as described in the Proposed Update will lead to recognition of losses that are not consistent with the economics of the underlying transactions. The Proposed Update requires an assessment of onerous provisions for each individual performance obligation within a contract without respect to whether the contract as a whole is profitable, which will result in liabilities recorded for contracts that are profitable as a whole. Companies generally do not negotiate contracts based on profitability of individual performance obligations, but aim to ensure the profitability of a contract as a whole. We believe the Board should modify the onerous contract obligation guidance to account for and allocate onerous obligations only when contracts as a whole are expected to result in a net liability.

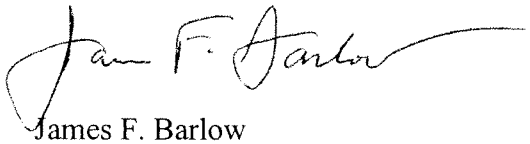
Best Estimate versus Probability-Weighted Amount: We strongly believe that the new concept introduced in the Proposed Update for using an estimated "probability-weighted amount" should be replaced with the well-known concept of "best estimate." The potential confusion to the users of financial statements that will be generated from the use of a proposed look-alike statistical method that is not applied in a statistically valid manner is totally inappropriate. Such a method would also infer significantly more accurate estimates in the minds of users which is clearly not the intention here if the Board moves revenue recognition in this direction.

Scope Questions: We would ask the Board to clarify how to treat collaboration or other risk-sharing type contracts with customers versus partners under the Proposed Update. Should such contracts be bifurcated between the cost sharing elements and the revenue sharing elements? Or should the contracts with partners be accounted for singularly under existing collaborations guidance and not be subject to this Proposed Update? We strongly urge the Board to add to the main body of the Proposed Update the information contained in *Basis for Conclusions* paragraph 17 in a format to clarify that collaboration arrangements with partners (as opposed to supplier-customer arrangements) is not subject to the principles in this Proposed Update.

Thank you for your consideration.

Sincerely,

Marc Veale
Assistant Corporate Controller
Allergan, Inc.



James F. Barlow
Senior Vice President,
Corporate Controller (Principal Accounting Officer)
Allergan, Inc.