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Mr. Timothy S. Lucas
Director of Research and Technical Activities
File Reference No. 194-B
Financial Accounting Standards Board
401 Merritt 7, P.O. Box 5116
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Dear Sir:

We appreciate the opportunity to respond to the Exposure Draft, Consolidated Financial Statements: Purpose and Policy. We are especially concerned about the consistency with which this proposed Statement will be applied, noting that the Board has defined just four presumptions of control as follows:

- (1) a majority voting interest in the election of a corporation's governing body or a right to appoint a majority of the members of its governing body
- (2) a large minority voting interest in the election of a corporation's governing body and no other party or organized group of parties has a significant voting interest
- (3) a unilateral ability to (a) obtain a majority voting interest in the election of a corporation's governing body or (b) obtain a right to appoint a majority of the corporation's governing body through the present ownership of convertible securities or other rights that are currently exercisable at the option of the holder and the expected benefit from converting those securities or exercising that right exceeds its expected cost and
- (4) the only general partner in a limited partnership and no other partner or organized group of partners has the current ability to dissolve the limited partnership or otherwise remove the general partner.

In addition, Paragraph 17 also notes, "the absence of one of those specific situations does not lead to a presumption that control is not present" and that these situations as identified are only a few of the most common ways of considering control. Further, evidence that demonstrates the absence of control can overcome the rebuttable presumptions of control.

It is our position that without further clarification of the presumptions of control and additional guidance surrounding other situations where control may exist, application of this proposed Statement will be subject to individual interpretation and, therefore, will not meet the intended purpose of the Statement, which is to improve the completeness, relevance, reliability and comparability of consolidated financial statements. In addition, we do not wholeheartedly agree with all of the presumptions as defined in the proposed Statement.

Issue 1: Definition of Control

We believe that the revised definition of control and the discussion of the characteristics of control and descriptive guidance do help clarify when one entity controls another entity to the extent that one of the four rebuttable presumptions are present. However, in the absence of these specific situations, application of the proposed Statement relies on individual interpretation of the definitions and guidance provided and the resulting conclusions may vary. The Statement also provides that the rebuttable presumptions of control may be overcome by evidence that demonstrates the absence of control, but it is unclear what evidence would be required to assert this position. It is our concern that individuals reviewing the same facts may weigh the evidence differently and thereby arrive at different conclusions.

For instance, in Example 5, Ability to Acquire a Majority Voting Interest through a Purchase Option, there are several characteristics of control, including a rebuttable presumption of control: the investor has a purchase option for all of the callable stock of the investee; the investee is required to hire the investor to perform all of the activities of the investee; the investee must use all of the proceeds from stock issuance and other income to pay the investor for performing the activities of the investee; the investee may not issue stock, pay dividends, borrow, merge, liquidate or sell assets until the purchase option expires; the investor is not required to provide additional funding after the purchase option expires; the investee's board of directors was selected by the investor and 4 of 5 members are directly or closely affiliated with the investor; and the chairman of the board is the CEO of the investor company. Almost all of the characteristics of control, as defined in the Statement, are present in this situation. These characteristics further support the rebuttable presumption of control that is present and support the conclusion that the investor does control the investee.

Would a reasonable person reach the same conclusion if a few of the facts in this example were different? Suppose the following assumptions are added to Example 5: the investee may solicit bids from other companies to perform some or all of the activities of the investee and the investee is not required to, but may use the investor to provide services; the investor must approve the company selected to perform the investee's activities and will not unreasonably withhold approval; the investor will propose the budget for the investee and the board of directors must approve this budget, and; the investee's board of directors is selected by the investee.

We believe that the investor would not be required to consolidate in this scenario based on our interpretation of the proposed Statement. The investor does have an option to purchase the callable stock of the investee, but ultimately the management and control of the day-to-day activities of the company reside with the investee through the investee's control of the board of directors. In addition, it appears that the investor relinquishes control in the suggestion that the investee may reasonably select another qualified company to perform operational activities. The investor's ability to propose the budget for the investee is subject to approval of the board of directors and, therefore, does not indicate that the investor is managing the investee through the budget process. Limiting the investee's ability to merge, liquidate, sell assets or raise capital is merely a means through which the investor is protecting the investment and not necessarily a measure to control the on-going daily management of the investee. Our conclusion is based on the investor's lack of presence in the operating aspects of the investee. However, reasonable people may reach different conclusions based on their individual interpretation and application of the Statement's guidance. Is the ability to propose a budget greater evidence of control than the ability to approve the budget? Does a limitation on the ability of an investee to merge, liquidate, sell assets or raise capital indicate control when the investor does not have the ability to select the board of directors? As such, we recommend that the Board provide guidance on the relative importance of the characteristics of control, perhaps in a weighted order of importance, to assist in the application of the Statement.

Issue 2: Implementation Guidance

For consistent reporting, we believe that it is necessary and desirable to have specific guidance in the form of rebuttable presumptions. We do not, however, agree that control should be presumed as described, but rather, stronger indications of control must be present to assert the presumptions. As discussed above, it appears that the proposed Statement allows significant latitude for interpretation and we would suggest further guidance to meet the Statement's objective of comparability in reporting.

Majority voting interest in the election of a corporation's governing body or a right to appoint a majority of the members of its governing body

It seems apparent that a majority voting interest would indicate the ability of one entity to control another entity. The proposed Statement asserts, however, that evidence may be presented to suggest that a majority interest may share decision-making powers with the minority voting interest in certain situations. The Statement falls short of describing any provisions or other specific evidence that would be necessary to overcome the majority voting interest presumption. Current guidance in EITF 96-16 provides clear terms for overcoming the presumption of control by a majority shareholder through specific points illustrated in the "Participating Rights" and "Factors to Consider" sections of the EITF. This Statement replaces the clear terms of the EITF with a model that requires significant interpretation and judgement.

Assume Company A enters into a joint venture agreement with Company B for a forty-nine per cent ownership interest and the board of directors of the joint venture is comprised of an equal number of representatives from Company A and Company B. In the event of an even split in a vote of the board of directors, the CEO of Company A would cast the deciding vote. We believe that Company A clearly overcomes the presumption of majority shareholder interest. This situation is specifically addressed in EITF 96-16 in the second point under "Factors to Consider" that discusses governance arrangements and the decision-making. Although, the proposed Statement suggests that this is the proper conclusion, it is difficult to support specifically within the guidance. We recommend that the Board provide specific criteria for situations in which control does not reside with the majority interest, similar to the guidance issued in EITF 96-16.

Large minority voting interest in the election of a corporation's governing body and no other party or organized group of parties has a significant voting interest

The proposed Statement defines effective control as control that is conferred by factors that by themselves do not provide legal control but when taken together give rise to decision-making ability. This definition is further clarified to say that a minority holding together with wide dispersion of all other voting shares confers effective control under certain circumstances. This presumption assumes that the majority interest will remain passive and will not exercise its ability to legally control in any given situation. This presumption also does not consider the intent of a minority investor, who may not be inclined to be involved in the daily management of an investee. In addition, the assessment of control in a minority interest situation is subject to individual interpretation of the essential facts of the minority relationship. What percentage of voting shares is considered to be a large minority? How should we determine whether or not shares are widely dispersed? We believe that the Board must clarify the factors that confer effective control to the minority voting shares in order for this presumption to be consistently applied. Further, we recommend that the Board consider restricting this rebuttable presumption to situations where the minority has successfully exercised its influence through clear actions and intent to elect the governing body.

Unilateral ability to (1) obtain a majority voting interest in the election of a corporation's governing body or (2) obtain a right to appoint a majority of the corporation's governing body through the present ownership of convertible securities or other rights that are currently exercisable at the option of the holder and the expected benefit from converting these securities or exercising that right exceeds its expected cost

The proposed Statement asserts that the unilateral ability to obtain a majority interest in the corporation's governing body is evidence of control and supercedes the presumption of majority voting interest in a corporation's governing body. This presumption is difficult to conceptualize from an investor's perspective, especially if the securities or rights are obtained as a measure to protect an investment and the investor does not have the intention, the adequate resources or the interest to manage the day-to-day activities of their investment. We believe that this presumption of assuming control is inappropriate until there are clear facts that an investor is indeed taking steps to exercise and assume control. For example, suppose an investor was issued preferred stock with future conversion rights to a fixed value (e.g. \$10 million) voting common stock, which would currently yield an insignificant minority interest in the investee. The investor has no intention of participating in the management of the investee. If the stock price of the investee decreases, the preferred stock would convert to an increased number of common shares and the investor may be forced to consolidate under this Statement. In this scenario, the increase in the investor's minority interest in the investee was outside of the investor's control and to force consolidation of the investee is inconsistent with the intent of the investor and, therefore, is inappropriate. We recommend that the Board include specific language in the Statement to consider management's intent and require action of the investor to exert control under this presumption.

Only general partner in a limited partnership and no other partner or organized group of partners has the current ability to dissolve the limited partnership or otherwise remove the general partner

Limited partners by definition are restricted in their participation in the management and control of a business, but do have certain rights to protect their assets. In the proposed Statement, it is noted that protective veto rights of the limited partners are generally not considered equivalent in power to a right to initiate or participate in policy decisions. Further guidance regarding veto power indicates that the number and dispersion of limited partners must be assessed to reach a conclusion of control by the general partner. Example 3, Creation of a Limited Partnership with a Single General Partner, attempts to provide guidance for assessing the number and dispersion of limited partners, but uses extreme situations (i.e. 3 limited partners and 100 limited partners). We recommend that the Board develop further the notion of number and dispersion of limited partners to clarify their position and ensure consistent implementation of this Statement. We also would like the Board to consider that this presumption of control is based on the inaction of the limited partners in exercising their potential ability to remove a general partner and that this presumption may be inappropriate.

Summary

The proposed Statement only provides four presumptions of control. All other relationships between entities are subject to individual interpretation of the definitions of control and the related guidance. In Paragraph 190, the Board notes that this consolidation policy "is likely to lead to greater comparability and neutrality of information provided by all entities". We believe that this will not be the result in practice as application of this Statement requires a significant amount of interpretation. We are also concerned about the necessity of defending our consolidation positions with the SEC, which may interpret and apply this guidance differently. In summary, we recommend that 1) the Board expand the second, third and fourth presumptions of control to require that the investor act in a manner to exert influence before control is presumed, and 2) the Board provide additional guidance for the application of the presumptions in conjunction with the

characteristics of control. Specific guidance regarding the relative importance of the characteristics of control in the assessment of the relationship between entities would also provide more consistent application of this Statement.

Issue 3: Transition and Implications for Interim Reporting

This proposed Statement is requiring retroactive application of the consolidation policy. The consolidation policy issue has been outstanding for several years and indeed it has been since 1995 when this issue was last addressed without conclusion. We believe that retroactive restatement is not necessary and will not provide additional value to users of financial information who have relied on these statements in the past. It is our position that the cost to accumulate this historical data would exceed the benefits derived from this information by financial statement users who have already made decisions based on the consolidated information presented prior to the effective date of this Statement. We are concerned about the lack of accurate quarterly information and believe that it would be sufficient to provide year-end comparative data in the year of adoption and interim comparative data thereafter.

We appreciate the opportunity to express our views and concerns in regards to this proposed Statement.

Sincerely,

ELITLILLY AND COMPANY

Arnold C. Hanish

Finance Director, Corporate Accounting

and Chief Accounting Officer