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Vice President and Controller

April 4, 2003

Ms. Annette Kimmitt
Senior Project Manager
International Accounting Standards Board
30 Cannon Street, London EC4M 6XH
United Kingdom

Subject: Exposure Draft of Proposed Amendments to IAS 38 *Intangible Assets*

Dear Ms. Kimmitt:

Pfizer welcomes the opportunity to comment on the Exposure Draft of Proposed Amendments to IAS 38 *Intangible Assets*. Pfizer discovers, develops, manufactures and markets leading prescription medicines for humans and animals and many of the world's best-known consumer brands. The Company's 2002 total revenues were $32.4 billion and its assets were over $46.3 billion. Pfizer supports the efforts of the IASB to improve standards of financial accounting and reporting and achieve international convergence. Our comments are summarized below and are more fully discussed in the attached document.

We are in general agreement with the specific proposals on which the Board requested comments and are pleased to see the continued effort towards the international

convergence of accounting standards. However, we have summarized below several specific elements of the proposed amendments which we feel may delay that progression.

We believe that it is vital that international accounting standards established by the IASB:

- Constitute a comprehensive, generally accepted basis of accounting;
- Be of high quality; and
- Can be rigorously interpreted and applied.

We are deeply concerned that certain of the proposals contained in the exposure draft cannot practically meet the third condition; that is, they subject the financial statements to the results of extremely subjective analyses and increase the potential for misleading or abusive accounting.

Capitalization of Acquired IPR&D Projects

We do not agree with the proposed requirement that acquired in-process research and development projects (IPR&D) that meet the definition of an intangible asset be capitalized. (Please know that we also do not agree with the recent tentative decision of the FASB that would call for the capitalization of acquired IPR&D assets that have no alternative future use.) Moreover, attempting to measure this item under an impairment model is simply not practicable. Predicting cash flow forecasts on products which are not proven is difficult.

Current best practices in the United States pharmaceutical industry for acquired IPR&D is prescribed in an AICPA Practice Aid, *Assets Acquired in a Business Combination to be Used in Research and Development Activities: A Focus on Software, Electronic Devices, and Pharmaceutical Industries* (the "Practice Aid"). The Practice Aid indicates the fair value ascribed to an asset acquired which will be used in R&D activities and which has no alternative future use be immediately expensed. One of the underlying concepts related in the Practice Aid is that there are remaining risks (e.g. technological, regulatory, etc.) associated with the IPR&D outside the control of an entity. Further, not only do we agree with the FASB in SFAS 2, *Accounting for Research and Development Costs* (SFAS

2), which states that "at the time most research and development costs are incurred the future benefits are at best uncertain," we have seen that it is very true in our business model. Alternatively stated, most R&D expenditures do not have a probable future benefit.

Based on the guidance prescribed in the Practice Aid, we believe that acquired IPR&D projects subject to regulatory approval do not meet the definition of an asset. Accordingly, we recommend that amounts ascribed to IPR&D in connection with allocating the purchase price in a business combination be expensed.

Capitalization of Internally Generated Intangible Assets

We agree with the requirement that expenditures for research activities be expensed as incurred but we do not agree with the requirement that all expenditures for development, that meet specified criteria, be capitalized as intangible assets. Specifically, we believe that all expenditures related to IPR&D projects subject to regulatory approval should be expensed as incurred until such approval is obtained.

None of the capitalization criteria set forth in the exposure draft, in the words of the FASB in SFAS 2, "lends itself to establishing a condition that could be objectively and comparably applied by all enterprises. Considerable judgment [would be] required to identify the point in the progress of a … development project at which a new or improved product or process is 'defined' or is determined to be 'technologically feasible,' 'marketable,' or 'useful.' Nor can the 'probability of future benefits' be readily assessed. A 'management decision' to proceed with production does not necessarily assure future benefits".

The pharmaceutical industry represents a compelling example of how tenuous the future benefits of R&D are. The 2003 Pharmaceutical Industry Profile published by the

Pharmaceutical Research and Manufacturers of America (and available for you reference at www.pharma.org) states that it takes an estimated 10 to 15 years to develop a new drug from the laboratory to approval by the Federal Drug Administration (FDA). Further, of 5,000 to 10,000 screened compounds, only 250 enter pre-clinical testing; 5 enter clinical testing; and only 1 is approved by the FDA. Given the realities of the outcome of most R&D projects, we find the argument that there are probable future benefits that are determinable with accuracy not sustainable.

We believe that the "probable economic benefits" in the definition of an asset, as discussed in our comments on Acquired IPR&D Projects above, cannot be determined with sufficient reliability to support other than expense as incurred treatment. We recommend convergence with SFAS 2 which requires costs of research *and* development to be expensed as incurred.

Subsequent Expenditures

We agree that all research expenditures be expensed as incurred but do not agree that subsequent development expenditures on acquired IPR&D subject to regulatory approval, that meet specified criteria, be capitalized as intangible assets. For the same reasons stated in our comments on Acquired IPR&D Projects above, we believe that all IPR&D expenditures should be expensed as incurred until the relevant risks associated with IPR&D are resolved.

Measurement of Intangible Assets Subsequent to Initial Recognition

We agree with the Benchmark Treatment that requires a recognized intangible asset to be carried at cost less accumulated amortization and impairment write-downs. However, we do not agree with the existence of an Allowed Alternative Treatment and we cannot support the concepts embodied by the Allowed Alternative Treatment.

The use of "Allowed Alternative Treatments" undermines the objectives of good and usable accounting standards. More specifically, the Allowed Alternative Treatment is based on utilizing a fair value method of accounting that will result in reporting temporary and perhaps volatile fluctuations in asset values. We believe that the use of alternative accounting treatments for the same accounting event results in a lack of comparability among entities; could greatly confuse the users of financial statements and would place an enormous updating burden on financial statement preparers.

We recommend that the Benchmark Treatment be the only treatment allowed and required.

Certain Disclosures

We believe that, in the interest of international convergence, the disclosure requirements for intangible assets should be consistent with the requirements of SFAS 142, *Goodwill and Other Intangible Assets* (SFAS 142).

We believe that detailed disclosures concerning certain balances, movements and underlying assumptions associated with recognized intangible assets should not be required due to the significant competitive harm that could result from such disclosures. We believe that additional, detailed information concerning intangible assets should not be required as much of that information could interfere with the competitive business practices of the company. We believe that the current disclosure rules, provided primarily through SFAS 142, are sufficient in these highly sensitive areas. Greater disclosure in these areas will likely compromise proprietary and highly confidential information of a company and could significantly impair the ability of the company to effectively compete in a market that is substantively dependent on intellectual property, such as the pharmaceutical industry.

We also believe that the proposed disclosures specifically relating to reconciling the beginning and ending carrying amounts of intangible assets will result in information

overload for financial statement users. We do not believe that financial statement users need all of this information, nor could they effectively process the information, if given.

Timing of Loss Recognition Associated with Retirements and Disposals of Intangible Assets

We believe that, in the interest of international convergence, the timing of loss recognition and the treatment of amortization expense for intangible assets held for disposal should be consistent with the guidance in Statement of Financial Accounting Standards No.144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (SFAS 144). SFAS 144 requires that a long-lived asset not be depreciated/amortized while it is classified as held for sale (disposal) and that it be measured at the lower of its carrying amount or fair value less cost to sell at the date it is classified as held for sale.

Timing of the Impairment Test of Indefinite-Lived Intangible Assets

We do not agree that the impairment test of indefinite-lived intangible assets should be required to be carried out at the end of each annual period. We believe that management bears ultimate responsibility for the financial statements and, therefore, management should determine when this annual impairment test should be carried out--after taking into consideration the level of effort and time commitment required for the test and in light of the entity's other commitments during the year. With the increased demand for more timely external reporting, we are concerned about the ability of organizations to meet their financial reporting deadlines while having to test what could be a large number of intangible assets at yearend, review and analyze the results and, as necessary, prepare the requisite disclosures based on those findings.

We recommend convergence with SFAS 142, which also requires an annual impairment test but does not specify when that impairment test should be carried out. We agree with the proposal to test goodwill for impairment annually without specifying when during the annual reporting period this test is to be carried out.

Our more specific comments to several of the items in the proposal are set forth in the attachment.

We appreciate your consideration of these comments. We would be happy to discuss these matters further or to meet with you if it would be helpful.

Sincerely,

Loretta V. Cangialosi

Loretta V. Cangialosi
Vice President and Controller

cc: David L. Shedlarz, Executive Vice President and Chief Financial Officer, Pfizer Inc
Alan G. Levin, Vice President-Finance, Pfizer Inc

Attachment

Detailed Response to the Proposed Amendments to IAS 38 Intangible Assets

Question 1 - Identifiability

The Exposure Draft proposes that an asset should be treated as meeting the identifiability criterion in the definition of an intangible asset when it is separable or arises from contractual or other legal rights (see proposed paragraphs 10 and 11 and paragraphs B6-B10 of the Basis for Conclusions).

Are the separability and contractual/other legal rights criteria appropriate for determining whether an asset meets the identifiability criterion in the definition of an intangible asset? If not, what criteria are appropriate, and why?

Pfizer Response to Question 1: We believe the guidance is appropriate.

Question 2 - Criteria for recognising intangible assets acquired in a business combination separately from goodwill

This Exposure Draft proposes that for an intangible asset acquired in a business combination, the probability recognition criterion will always be satisfied and, with the exception of an assembled workforce, sufficient information should always exist to measure its fair value reliably (see proposed paragraphs 29-32 and paragraphs B11-B15 of the Basis for Conclusions). Therefore, as proposed in ED 3, an Exposure Draft of a proposed International Financial Reporting Standard Business Combinations, an acquirer should recognise, at the acquisition date and separately from goodwill, all of the acquiree´s intangible assets, excluding an assembled workforce, that meet the definition of an intangible asset (see proposed paragraphs 36, 43 and 44 of ED 3).

Do you agree that, with the exception of an assembled workforce, sufficient information can reasonably be expected to exist to measure reliably the fair value of an intangible

asset acquired in a business combination? If not, why not? The Board would appreciate respondents outlining the specific circumstances in which the fair value of an intangible asset acquired in a business combination could not be measured reliably.

Pfizer Response to Question 2:

We agree with the criteria for recognizing intangible assets acquired in a business combination separately form goodwill. However, we do not agree with capitalizing amounts ascribed to acquired in-process research and developments projects ("IPR&D")

Current best practices in the United States pharmaceutical industry for acquired IPR&D is prescribed in an AICPA Practice Aid, *Assets Acquired in a Business Combination to be Used in Research and Development Activities: A Focus on Software, Electronic Devices, and Pharmaceutical Industries* (the "Practice Aid"). The Practice Aid indicates the fair value ascribed to an asset acquired which will be used in R&D activities and which has no alternative future use be immediately expensed. One of the underlying concepts related in the Practice Aid is that there are remaining risks (e.g. technological, regulatory, etc.) associated with the IPR&D outside the control of an entity.

We believe that IPR&D projects, whether acquired or internally developed, do not meet the definition of an asset in Statement of Financial Accounting Concepts No. 6, *Elements of Financial Statements (CON 6)* which states that "Assets are probable[1] future economic benefits obtained or controlled by a particular entity as a result of past transactions or events."

The Practice Aid concluded that "many of the assets acquired to be used in R&D activities would not satisfy a requirement that there be a probable future economic benefit

[1] CON 6 Definition of Probable - *Probable* is used with its usual general meaning, rather than in a specific accounting or technical sense (such as that in FASB Statement No. 5, *Accounting for Contingencies*, par. 3), and refers to that which can reasonably be expected or believed on the basis of available evidence or logic but is neither certain nor proved (*Webster's New World Dictionary of the American Language*, 2d college ed. [New York Simon and Schuster 1982], p. 1132). Its inclusion in the definition is intended to acknowledge that business and other economic activities occur in an environment characterized by uncertainty in which few outcomes are certain (pars. 44-48).

for many of the same reasons that the FASB concluded in SFAS 2 that R&D costs should not be capitalized as assets."

Based on the guidance prescribed in the Practice Aid and U.S. GAAP, we believe that acquired IPR&D projects subject to regulatory approval do not meet the definition of an asset under U.S.GAAP based on the uncertainty of deriving future economic benefits. Accordingly, we recommend that amounts ascribed to acquired IPR&D in connection with allocating the purchase price in a business combination be expensed. Furthermore, we believe that recognizing acquired IPR&D projects as assets will inevitably result in subsequent impairment charges due to the incomplete nature of IPR&D.

Question 3 - Indefinite useful life

The Exposure Draft proposes to remove from IAS 38 the rebuttable presumption that an intangible asset´s useful life cannot exceed twenty years, and to require its useful life to be regarded as indefinite when, based on an analysis of all of the relevant factors, there is no foreseeable limit on the period of time over which the asset is expected to generate net cash inflows for the entity (see proposed paragraphs 85-88 and paragraphs B29-B32 of the Basis for Conclusions).

Is this appropriate? If not, under what circumstances, if any, should an intangible asset be regarded as having an indefinite useful life?

Pfizer Response to Question 3: We believe the guidance is appropriate.

Question 4 - Useful life of intangible asset arising from contractual or other legal rights

The Exposure Draft proposes that if an intangible asset arises from contractual or other legal rights that are conveyed for a limited term that can be renewed, the useful life shall include the renewal period(s) only if there is evidence to support renewal by the entity

without significant cost (see proposed paragraphs 91 and 92 and paragraphs B33-B35 of the Basis for Conclusions).

Is this an appropriate basis for determining the useful life of an intangible asset arising from contractual or other legal rights that are conveyed for a limited term that can be renewed? If not, under what circumstances should the useful life include the renewal period(s)?

Pfizer Response to Question 4: We believe the guidance is appropriate.

Question 5 - Non-amortisation of intangible assets with indefinite useful lives

The Exposure Draft proposes that an intangible asset with an indefinite useful life should not be amortised (see proposed paragraphs 103 and 104 and paragraphs B36-B38 of the Basis for Conclusions).

Is this appropriate? If not, how should such assets be accounted for after their initial recognition?

Pfizer Response to Question 5:

We agree that an intangible asset with an indefinite useful life should not be amortized. However, we do not agree with paragraph 104 (a) that these assets be tested for impairment at the end of each annual reporting period.

We note that paragraph 8A (a) of the ED calls for "impairment testing" of indefinite-lived intangible assets at the end of each annual reporting period: "Irrespective of whether there is any indication of impairment, an entity shall also estimate at the end of each annual reporting period the recoverable amount of an intangible asset with an indefinite useful life or an intangible asset not yet available for use." We note that Statement of Financial Accounting Standards, Goodwill and Other Intangible Assets (SFAS 142), paragraph 17, "An intangible asset that is not subject to amortization shall be tested for impairment annually, or more frequently if events or changes in circumstances indicate

that the asset might be impaired", also requires an annual impairment test but does not specify when that impairment test should be carried out. We believe that management should determine when the annual impairment test of indefinite-lived intangible assets should be performed.

Further, the annual impairment test for indefinite-lived intangible assets typically requires the use of external valuation consultants and can be efficiently performed in conjunction with the annual impairment test for goodwill. Management should be able to evaluate the appropriate time during the annual reporting period to perform the test, taking into consideration the level of effort and time commitment required for the test in light of the entity's other commitments during the year. Moreover, our U.S. Regulators, the Securities and Exchange Commission, are implementing accelerated filing deadlines for annual reports to 60 days after year end. We believe that this requirement will put undue stress on entities at this critical time of the year and may result in rushing through this important evaluation and substantiation process.

Additional Comments

We also have the following comments on certain elements of the proposed amendments of IAS 38:

Capitalization of Internally Generated Intangible Assets

We agree with the requirement that expenditures for research be expensed as incurred (paragraph 46) but we do not agree with the requirement that all expenditures for development, that meet specified criteria, be capitalized as intangible assets (paragraph 49). Specifically, expenditures related to IPR&D projects subject to regulatory approval should be expensed as incurred until such approval is obtained.

We believe that the "probable economic benefits" in the definition of an asset, as discussed in our comments on Acquired IPR&D Projects above, cannot be determined

with sufficient reliability for IPR&D projects subject to regulatory approval to support other than expense as incurred treatment.

We recommend convergence with SFAS 142, paragraph 10: "Costs of internally developing, maintaining, or restoring intangible assets (including goodwill) that are not specifically identifiable, that have indeterminate lives, or that are inherent in a continuing business and related to an entity as a whole, shall be recognized as an expense when incurred."

Subsequent Expenditures

We agree that all research expenditures be expensed as incurred but do not agree that subsequent development expenditures on acquired IPR&D subject to regulatory approval, that meet specified criteria, be capitalized as intangible assets (paragraphs 67/68).

We believe that the "probable economic benefits" in the definition of an asset, as discussed in our comments on Acquired IPR&D above, cannot be determined with sufficient reliability for IPR&D projects subject to regulatory approval to support other than expense as incurred treatment.

We also note that paragraph 49, allowing recognition of development expenditures as intangible assets, is inconsistent with the aforementioned AICPA Practice Aid in which concluded that "many of the assets acquired to be used in R&D activities would not satisfy a requirement that there be a probable future economic benefit for many of the same reasons that the FASB concluded in SFAS 2 that R&D costs should not be capitalized as assets."

We recommend convergence with SFAS 142, paragraph 10: "Costs of internally developing, maintaining, or restoring intangible assets (including goodwill) that are not specifically identifiable, that have indeterminate lives, or that are inherent in a continuing business and related to an entity as a whole, shall be recognized as an expense when incurred."

Measurement of Intangible Assets Subsequent to Initial Recognition

We agree with the Benchmark Treatment that requires an intangible asset to be carried at cost less accumulated amortization and impairment write-downs (paragraph 69) but we do not agree with the Allowed Alternative Treatment (paragraphs 70-84).

We believe that the use of alternative accounting treatments for the same accounting event results in a lack of comparability among entities. We support the use of alternative treatments to account for different events, such as the availability of alternative depreciation methods to reflect the manner in which an entity utilizes an asset. Furthermore, we believe that accounting for intangible assets utilizing a fair value method results in reporting temporary and perhaps volatile fluctuations in asset values.

We also do not agree with the requirement under the Allowed Alternative Treatment that if an intangible asset (in a class of revalued intangible assets) cannot be revalued because there is no active market, it should be carried at its revalued amount at the date of the last revaluation by reference to the active market less any subsequent accumulated amortization and impairment losses. Furthermore, if the fair value of the asset can be determined by reference to an active market at a subsequent measurement date, the allowed alternative treatment is applied from that date. We do not believe that an asset should be reported utilizing different methods at different times (paragraphs 72, 78, 79, and 81).

We also find that the revaluation requirements (paragraphs 82 to 84) can result in many burdensome and complex accounting steps.

We recommend that the Benchmark Treatment be the only treatment allowed and required. We believe that, in the interest of international convergence, the accounting for intangible assets should be consistent with the guidance in SFAS 142.

Timing of Loss Recognition Associated with Retirements and Disposals

We believe that, in the interest of international convergence, the timing of loss recognition and the treatment of amortization expense for assets held for disposal should

be consistent with the guidance in Statement of Financial Accounting Standards No.144, *Accounting for the Impairment or Disposal of Long-Lived Assets (SFAS 144)*.

Paragraph 112 of the ED requires amortization of an intangible asset with a finite useful life to continue while it is held for sale (disposal) and paragraph 109 requires gain or loss to be recognized on disposal. We note that under SFAS 144 (paragraph 34) a long-lived asset is not depreciated/amortized while it is classified as held for sale and it is measured at the lower of its carrying amount or fair value less cost to sell at the date it is classified as held for sale. Under SFAS 144, the anticipated loss on disposal is recognized at the classification date.

Disclosure

We do not agree that an entity should be required to disclose all of the items in proposed paragraph 113. Specifically, we do not believe that the reconciliation for intangible assets of the carrying amount at the beginning and end of the period in sub-paragraph (e) is necessary for most entities.

In addition, we believe that the disclosures required by paragraph 117 will result in information overload for financial statement users. We do not believe that financial statement users need nor want to know all the information proposed for disclosure; for example, justifying the assignment of an indefinite life to an intangible asset. We believe that, for most entities, management's decisions, possibly arrived at in consultation with valuation consultants, and audited by external auditors are sufficient for financial statement users without a need for further details.

We believe that detailed disclosures concerning certain balances, movements and underlying assumptions associated with recognized intangible assets should not be required due to the significant competitive harm that could result from such disclosures. We believe that additional, detailed information concerning intangible assets should not be required as much of that information could interfere with the competitive business practices of the company. We believe that the current disclosure rules, provided primarily through SFAS 142, are sufficient in these highly sensitive areas. Greater disclosure in these areas will likely compromise proprietary and highly confidential

information of a company and could significantly impair the ability of the company to effectively compete in a market that is substantively dependent on "secrets," such as the pharmaceutical industry.

Finally, we do not agree with the Allowed Alternative Treatment as discussed above, and find the requirements of paragraph 119 regarding fair values and revaluations to be excessive. We believe that, in the interest of international convergence, the disclosure requirements for intangible assets should be consistent with the requirements of SFAS 142.