

Eli Lilly and Company
Lilly Corporate Center
Indianapolis, IN 46285
U.S.A.

August 17, 2009

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F. Street, N.E.
Washington, DC 20549-1090

Re: File No. S7-10-09
Release Nos. 33-9046, 34-60089, IC-28765 (the "Release")
Proposed rule: Facilitating Shareholder Director Nominations

Dear Ms. Murphy:

Eli Lilly and Company is a global, NYSE-listed company based in Indianapolis, Indiana. We submit this letter in response to the Commission's request for comments on the Release referenced above.

We support the comments provided by the Society of Corporate Secretaries and Governance Professionals (the "Society") in a letter dated August 13, 2009. In addition, we have signed and support the comments provided by a group of corporate secretaries and governance professionals on behalf of their respective companies dated August 17, 2009. This letter serves as a supplement to the comments provided by both groups.

In addition to the comments provided in the letters referenced above, we believe that it is important to craft the new rules to address the unintended consequence of promoting short-term decision making and the possible use of Rule 14a-11 to accomplish a change in control. It is clear from the Release that the goal of the new rules is not to create another mechanism to execute a change in control, but to create a process that empowers long-term, substantial shareholders to nominate credible board candidates. Although our view is that private ordering under state corporate law is the better way to address proxy access, should Rule 14a-11 be implemented, we believe that in order to be successful, the following issues should be addressed.

- I. **The proposed rule may result in actions by shareholders, their nominees, and companies that focus on short-term issues at the expense of the long-term interests of companies and their shareholders.**

1. The share ownership requirements for large accelerated filers should be increased.

We agree with the Society's comment that the proposed ownership requirements do not appropriately balance the Commission's stated goal of increasing shareholders' participation in the director election process against the cost of disruption to companies, and we support the 5% (sole shareholder) and 10% (shareholder group) thresholds recommended by the Society and other commentators.

For two reasons, we believe higher thresholds are necessary to avoid adopting a rule that is counterproductive to the goal of long-term value creation for the benefit of all shareholders:

- **Election contests with little chance of success will distract directors from overseeing strategy, performance, and risk management.** Directors' time is finite, and time spent on election contests by nominees who have little chance of gaining meaningful support is time spent away from the directors' most important duties – overseeing the company's development and implementation of its long-term strategy and the management of risk.
- **Higher thresholds will promote a healthy self-regulation by shareholders.** The 5% / 10% thresholds we support would serve as a shareholder self-regulation mechanism, enabling shareholders to cost-effectively "weed out" potential nominees who espouse narrow, short-term views that are inconsistent with long-term value creation and therefore cannot garner the advance support of a substantial proportion of the shareholder base.

2. Shareholder proponents should be required to have a net long stake in the company for two to three years.

We agree with the Commission's view that "long-term shareholders are more likely to have interests that are better aligned with other shareholders and are less likely to use the rule solely for short-term gain."¹ However, we believe that the proposed one-year holding period is inadequate to meet the intent of this requirement. In addition, as demonstrated in the recent enforcement action against Perry Corp.,² shareholders can hedge or otherwise separate their economic interest in the company from their right to vote. Absent a long-term economic interest, the right to nominate director candidates is inappropriate and less likely to result in nominees aligned with the interests of long-term shareholders. As a result, we believe that shareholders should be required to have a net long position in the company's stock in an amount meeting or exceeding the ownership requirement, held consistently for two to three years.

We believe a proponent should be required to hold this position through the date of the annual meeting (and provide documentation of that position up to a date within a few days of the meeting),

¹ Release, pp. 50-51

² *In the Matter of Perry Corp.*, Securities Exchange Act of 1934 Release No. 60351; Investment Advisers Act of 1940 Release No. 2907; Administrative Proceeding File No. 3-13561 (Jul. 21, 2009)

and express an intent to continue to hold that position through at least the first year of their nominee's service on the board.

Finally, the nominating shareholder should be required to disclose all of his or her positions in the company's stock, rather than just long positions, and disclose any arrangement related to voting or economic interests in company stock. This disclosure provides transparency about the nominating shareholder's true equity position in the company, which is important information for the other shareholders voting on a nominee.

3. The proposed rule should be revised to support collaboration between nominating shareholders, their nominees, and the nominating committee of the board.

Boards of most large, publicly-traded companies, including Lilly, spend a substantial amount of time identifying directors with specific capabilities and creating a board that has a balance of skills and expertise and can effectively represent the long-term interests of all shareholders. For example, our company seeks to maintain a board comprised of members with medical and scientific knowledge, an understanding of global business operations and strategy, sales and marketing experience, financial expertise, and the ability to identify and address risk; other industries have other needs, some of which are very specific or mandated by law. In addition, it is important that the board represent a diversity of backgrounds and experiences. The NYSE has identified the role of the nominating committee as "central to the effective functioning of the board."³ We believe the proposed Rule 14a-11 should be revised to include a role for the nominating committee of the board in reviewing director candidates, both because the nominating committee has a fiduciary duty to all shareholders and because the committee's judgment is relevant to shareholder voting decisions.

It is very possible that a shareholder nominee will be well-qualified for service on the board, and it is in the best interests of both management and shareholders to identify such candidates and possibly put them forward with the support of the company's board. Nominees should be required to submit the same information required of management nominees, including the new disclosure proposed in "Proxy Disclosure and Solicitation Enhancements" (Release No. 33-9052, dated July 10, 2009), to allow the nominating committee and shareholders to evaluate their suitability to join the board.

Shareholder nominees should count towards the cap on shareholder nominees, even if endorsed by management; otherwise there is an incentive not to endorse a qualified candidate in order to avoid being required to include additional nominees in the proxy statement. Further, shareholder nominees should continue to count towards this cap for a period beyond their first term, to encourage the nominating committee to consider re-nominating a successful shareholder-nominated director.

Changes such as those described above would increase the chances of well-qualified shareholder nominees being elected, potentially with management support, and serving successfully on the board. This approach allows for less disruption to the functioning of the board and less expense to the

³ NYSE Listed Company Manual, commentary on Rule 303A.04

company, through informed shareholder voting and smooth integration of shareholder nominees, should they be elected.

4. Additional disclosures about shareholder nominees are needed to inform shareholder votes.

If the intent of including shareholder proponent nominees in the company's proxy statement is to set these nominees up for successful elections and board service, significantly more information must be provided to shareholders to allow them to cast informed votes. We believe that shareholder nominees should be required to provide the information required of other director nominees, including the new disclosures proposed in Release No. 33-9052 and disclosure of any relationships between the nominee and the nominating shareholder(s). Providing additional information about a nominee's skills, experience, and relationships with the nominating shareholder(s) will allow shareholders to make an informed decision about the director and his or her potential fit on the board. This increases the chances that well-qualified candidates are elected, that less-qualified candidates are not, and that elected shareholder nominees would serve successfully and be reelected in the future.

II. The proposed rule may inadvertently foster an effective change in control of a company. The rule should be revised to clearly distinguish the right to nominate a director from the process to undertake a proxy contest.

1. Shareholders should be allowed to nominate only one candidate.

We agree with the Society's comment that each shareholder or nominating group should be able to submit only one nominee. This approach is consistent with the Commission's intent that Rule 14a-11 be available only to shareholders that "are not seeking to change the control of the issuer."⁴ The purpose of the proposed rule is to facilitate "the exercise of [a shareholder's] fundamental right to nominate and elect members of the company boards directors."⁵ We believe that, particularly given recent advances in corporate governance, alternate strategies successfully used to put pressure on issuers (such as "vote no" campaigns, shareholder proposals, and increased public scrutiny), and the availability of eProxy to conduct a proxy solicitation under Rule 14a-16, this purpose is met by the ability of a shareholder to seat a single representative on the board. In addition, we feel that replacing 25 percent of the board membership will result in a significant change in the make-up of the board and could form the groundwork for a change in control, despite the stated intentions of the nominating shareholder. The right to put forward a "bloc" of directors is similar in effect to putting forward a "short slate", which is more appropriately achieved through a short slate proxy contest under Rule 14a-4(d). In addition, this limitation would potentially leave room for nominations by more than one shareholder or group of shareholders.

⁴ Release, p. 27

⁵ Release, p. 7

2. Nominees should be independent of their proponents.

We believe that shareholder nominees should be independent of their nominator, as originally proposed by the Commission in 2003.⁶ Consistent with the stated goal that Rule 14a-11 should only be available to shareholders who do not intend to seek a change in control, this requirement would increase the likelihood that a nominee is not bound by any obligation to the nominating shareholder and can fulfill his or her fiduciary duties to all shareholders. It is also logical that a candidate nominated by an unrelated shareholder is more likely to garner the support of other shareholders than a candidate who is put forward by him or herself, a family member, a client, or an employer.

3. Shareholder representations in Schedule 14N should be expanded.

We believe that all nominating shareholders should be required to represent in Schedule 14N that they will not seek to change control of the company or gain more than one seat on the board for at least one year beyond the relevant election of directors. If the nominee is elected and, during the first year after the election, any of the nominating shareholders changes their intent, the shareholder should be required to amend its filing and the director so nominated should be required to resign from the board.

4. Proposed Rule 14a-11 should specify that shareholder nominees need not be included in the company's proxy statement in the event of a proxy contest, including a short-slate proxy fight, or other form of contest for control.

The inclusion of nominees under Rule 14a-11 should not be required if the company is the subject of a traditional proxy contest, whether a full slate or short slate, in the same year, or is otherwise subject to a contest for control. Given the Amylin Pharmaceuticals no-action letter from earlier this year, a dissident shareholder could "round out" a short slate by including shareholder nominees and actively solicit support for these nominees. As a result, nominees included under Rule 14a-11 could become part of an effort to complete a change in control, which is counter to the intent of the rule. In addition, multiple proposed slates of directors, along with alternative nominations by shareholders, have the potential to cause confusion for voting shareholders.

⁶ Release, p. 68

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5. As stated above, nominating shareholders should demonstrate long-term, net long holdings of company stock and provide additional disclosures about the qualifications of the nominee.

These requirements create a legitimate threshold to entry, avoiding the likelihood that stockholders with short-term or special interests can successfully nominate a shareholder candidate and facilitating informed voting decisions by shareholders. The disclosures suggested above, and in the other letters we have referenced, clarify the interests of the nominating shareholder and the qualifications of the nominee, which allows shareholders to evaluate the legitimacy of the candidate.

Thank you for the opportunity to provide comment on the Release and for the comprehensive work that went into preparing it.

Sincerely,

A handwritten signature in black ink, appearing to read "J. B. Lootens", with a long horizontal flourish extending to the right.

James B. Lootens
Secretary and Deputy General Counsel