SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

Quarterly Report Under Section 13 or 15(d) of the Securities Exchange Act of 1934

FOR THE QUARTER ENDED SEPTEMBER 30, 2006

COMMISSION FILE NUMBER 001-6351

ELI LILLY AND COMPANY

(Exact name of Registrant as specified in its charter)

INDIANA	35-0470950
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

LILLY CORPORATE CENTER, INDIANAPOLIS, INDIANA 46285
(Address of principal executive offices)

Registrant's telephone number, including area code (317) 276-2000

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months and (2) has been subject to such filing requirements for the past 90 days.

Yes ☑ No o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer.

Large accelerated filer ☑ Accelerated filer o Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No ☑

The number of shares of common stock outstanding as of October 20, 2006:

Class	Number of Shares Outstanding
Common	1,131,588,452

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

CONSOLIDATED CONDENSED STATEMENTS OF INCOME
(Unaudited)

ELI LILLY AND COMPANY AND SUBSIDIARIES

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
	(Dollars in millions except per-share data)			
Net sales	$ 3,864.1	$ 3,601.1	$ 11,445.7	$ 10,766.2
Cost of sales	860.4	845.7	2,527.5	2,576.0
Research and development	755.7	751.0	2,271.3	2,215.6
Marketing and administrative	1,198.2	1,070.9	3,579.0	3,307.4
Asset impairments, restructuring, and other special charges	—	—	—	1,073.4
Other income — net	(56.0)	(85.0)	(135.1)	(229.0)
	2,758.3	2,582.6	8,242.7	8,943.4
Income before income taxes	1,105.8	1,018.5	3,203.0	1,822.8
Income taxes	232.2	224.1	672.6	543.8
Net income	$ 873.6	$ 794.4	$ 2,530.4	$ 1,279.0
Earnings per share — basic	$ .80	$ .73	$ 2.33	$ 1.18
Earnings per share — diluted	$ .80	$ .73	$ 2.33	$ 1.17
Dividends paid per share	$ .40	$ .38	$ 1.20	$ 1.14

See Notes to Consolidated Condensed Financial Statements.

CONSOLIDATED CONDENSED BALANCE SHEETS

ELI LILLY AND COMPANY AND SUBSIDIARIES

	September 30, 2006 (Unaudited)	December 31, 2005
	(Dollars in millions)	
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 2,169.9	$ 3,006.7
Short-term investments	1,448.6	2,031.0
Accounts receivable, net of allowances of $73.1 (2006) and $62.5 (2005)	2,077.9	2,313.3
Other receivables	399.6	448.4
Inventories	2,199.8	1,878.0
Deferred income taxes	731.2	756.4
Prepaid expenses	744.2	362.0
TOTAL CURRENT ASSETS	9,771.2	10,795.8
OTHER ASSETS		
Prepaid pension	2,450.1	2,419.6
Investments	1,294.5	1,296.6
Sundry	2,182.2	2,156.3
	5,926.8	5,872.5
PROPERTY AND EQUIPMENT		
Land, buildings, equipment, and construction-in-progress	13,731.7	13,136.0
Less allowances for depreciation	(5,516.3)	(5,223.5)
	8,215.4	7,912.5
	$ 23,913.4	$ 24,580.8
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Short-term borrowings	$ 334.2	$ 734.7
Accounts payable	630.6	781.3
Employee compensation	454.3	548.8
Dividends payable	—	436.5
Income taxes payable	725.2	884.9
Other current liabilities	1,738.5	2,330.1
TOTAL CURRENT LIABILITIES	3,882.8	5,716.3
LONG-TERM DEBT	4,553.3	5,763.5
DEFERRED INCOME TAXES	847.8	695.1
OTHER NONCURRENT LIABILITIES	1,574.8	1,614.0
SHAREHOLDERS' EQUITY		
Common stock	707.6	706.9
Additional paid-in capital	3,482.3	3,323.8
Retained earnings	11,692.5	10,027.2
Employee benefit trust	(2,635.0)	(2,635.0)
Deferred costs — ESOP	(102.5)	(106.3)
Accumulated other comprehensive income (loss)	12.4	(420.6)
	13,157.3	10,896.0
Less cost of common stock in treasury	102.6	104.1
	13,054.7	10,791.9
	$ 23,913.4	$ 24,580.8

See Notes to Consolidated Condensed Financial Statements.

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(Unaudited)

ELI LILLY AND COMPANY AND SUBSIDIARIES

	Nine Months Ended September 30,	
	2006	2005
	(Dollars in millions)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 2,530.4	$ 1,279.0
Adjustments to reconcile net income to cash flows from operating activities:		
Changes in operating assets and liabilities	(1,318.6)	(1,796.0)
Depreciation and amortization	628.2	501.3
Stock-based compensation expense	274.3	309.5
Change in deferred taxes	130.5	(205.0)
Asset impairments, restructuring, and other special charges, net of tax	—	979.7
Other, net	(126.6)	30.8
NET CASH PROVIDED BY OPERATING ACTIVITIES	2,118.2	1,099.3
CASH FLOWS FROM INVESTING ACTIVITIES		
Net purchases of property and equipment	(667.8)	(878.5)
Net change in short-term investments	580.4	833.1
Purchase of noncurrent investments	(1,218.7)	(271.9)
Proceeds from sales and maturities of noncurrent investments	1,135.1	327.0
Other, net	124.4	(216.4)
NET CASH USED IN INVESTING ACTIVITIES	(46.6)	(206.7)
CASH FLOWS FROM FINANCING ACTIVITIES		
Dividends paid	(1,301.5)	(1,245.7)
Purchases of common stock	(122.1)	—
Issuances of common stock under stock plans	44.2	71.2
Net change in short-term borrowings	(1.8)	(1,984.6)
Net (repayments) issuances of long-term debt	(1,599.0)	1,998.0
Other, net	6.3	33.2
NET CASH USED IN FINANCING ACTIVITIES	(2,973.9)	(1,127.9)
Effect of exchange rate changes on cash and cash equivalents	65.5	(160.3)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(836.8)	(395.6)
Cash and cash equivalents at January 1	3,006.7	5,365.3
CASH AND CASH EQUIVALENTS AT SEPTEMBER 30	$ 2,169.9	$ 4,969.7

See Notes to Consolidated Condensed Financial Statements.

CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

ELI LILLY AND COMPANY AND SUBSIDIARIES

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
	(Dollars in millions)			
Net income	$ 873.6	$ 794.4	$ 2,530.4	$ 1,279.0
Other comprehensive income (loss) [1]	132.3	48.2	433.0	(468.7)
Comprehensive income	$ 1,005.9	$ 842.6	$ 2,963.4	$ 810.3

[1] The significant components of other comprehensive income were gains of $123.4 million and $346.7 million from foreign currency translation adjustments for the three months and nine months ended September 30, 2006, respectively, and losses of $421.4 million from foreign currency translation adjustments for the nine months ended September 30, 2005.

See Notes to Consolidated Condensed Financial Statements.

SEGMENT INFORMATION

We operate in one significant business segment — pharmaceutical products. Operations of our animal health business segment are not material and share many of the same economic and operating characteristics as our pharmaceutical products. Therefore, they are included with pharmaceutical products for purposes of segment reporting. Our business segments are distinguished by the ultimate end user of the product: humans or animals. Performance is evaluated based on profit or loss from operations before income taxes. Income before income taxes for the animal health business was $47.8 million and $55.7 million for the quarters ended September 30, 2006 and 2005, respectively, and $122.9 million and $143.0 million for the nine months ended September 30, 2006 and 2005, respectively.

SALES BY PRODUCT CATEGORY

Worldwide sales by product category for the three months and nine months ended September 30, 2006 and 2005 were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
	(Dollars in millions)			
Net sales — to unaffiliated customers				
Neurosciences	$ 1,676.1	$ 1,514.9	$ 4,869.4	$ 4,490.2
Endocrinology	1,221.0	1,115.9	3,680.9	3,402.2
Oncology	511.8	456.9	1,477.6	1,312.2
Animal health	216.2	215.7	615.5	612.3
Cardiovascular	117.3	135.8	387.9	459.6
Anti-infectives	58.5	104.7	216.0	326.7
Other pharmaceuticals	63.2	57.2	198.4	163.0
Net sales	$ 3,864.1	$ 3,601.1	$ 11,445.7	$ 10,766.2

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

BASIS OF PRESENTATION

We have prepared the accompanying unaudited consolidated condensed financial statements in accordance with the requirements of Form 10-Q and, therefore, they do not include all information and footnotes necessary for a fair presentation of financial position, results of operations, and cash flows in conformity with accounting principles generally accepted in the United States (GAAP). In our opinion, the financial statements reflect all adjustments (including those that are normal and recurring) that are necessary for a fair presentation of the results of operations for the periods shown. In preparing financial statements in conformity with GAAP, we must make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosures at the date of the financial statements and during the reporting period. Actual results could differ from those estimates.

The information included in this Quarterly Report on Form 10-Q should be read in conjunction with our consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2005.

CONTINGENCIES

We are engaged in the following patent litigation matters brought pursuant to procedures set out in the Hatch-Waxman Act (the Drug Price Competition and Patent Term Restoration Act of 1984):

- Dr. Reddy's Laboratories, Ltd. (Reddy), Teva Pharmaceuticals, and Zenith Goldline Pharmaceuticals, Inc., which was subsequently acquired by Teva Pharmaceuticals (together, Teva), each submitted abbreviated new drug applications (ANDAs) seeking permission to market generic versions of Zyprexa® prior to the expiration of our relevant U.S. patent (expiring in 2011) and alleging that this patent was invalid or not enforceable. We filed lawsuits against these companies in the U.S. District Court for the Southern District of Indiana, seeking a ruling that the patent is valid, enforceable, and being infringed. The district court ruled in our favor on all counts on April 14, 2005. We are now awaiting a decision by the Court of Appeals for the Federal Circuit, which on April 6, 2006, heard Reddy's and Teva's respective appeals of this ruling. We are confident Reddy's and Teva's claims are without merit and we expect to prevail. However, it is not possible to predict or determine the outcome of this litigation, and accordingly, we can provide no assurance that we will prevail on appeal. An unfavorable outcome would have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

- Barr Laboratories, Inc. (Barr), submitted an ANDA in 2002 seeking permission to market a generic version of Evistaâ prior to the expiration of our relevant U.S. patents (expiring in 2012-2017) and alleging that these patents are invalid, not enforceable, or not infringed. In November 2002, we filed a lawsuit against Barr in the U.S. District Court for the Southern District of Indiana, seeking a ruling that these patents are valid, enforceable, and being infringed by Barr. Teva has also submitted an ANDA seeking permission to market a generic version of Evista. In June 2006, we filed a lawsuit against Teva in the U.S. District Court for the Southern District of Indiana, seeking a ruling that our relevant U.S. patents (expiring in 2012-2014) are valid, enforceable, and being infringed by Teva. No trial date has been set in either case. We believe Barr's and Teva's claims are without merit and we expect to prevail. However, it is not possible to predict or determine the outcome of this litigation, and accordingly, we can provide no assurance that we will prevail. An unfavorable outcome could have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

- Sicor Pharmaceuticals, Inc. (Sicor), a subsidiary of Teva, submitted ANDAs in November 2005 seeking permission to market generic versions of Gemzar® prior to the expiration of our relevant U.S. patents (expiring in 2010 and 2013), and alleging that these patents are invalid. In February 2006, we filed a lawsuit against Sicor in the U.S. District Court for the Southern District of Indiana, seeking a ruling that these patents are valid and are being infringed by Sicor. In response to our lawsuit, Sicor filed a declaratory judgment action in the U.S. District Court for the Central District of California. The California action has since been dismissed. In September 2006, we received notice that Mayne Pharma (USA) Inc. (Mayne) filed a similar ANDA for Gemzar. In October 2006, we filed a lawsuit against Mayne in the Southern District of Indiana in response to the ANDA filing. We are awaiting the filing of an answer to our complaint against Mayne. In October 2006, we received notice that Sun Pharmaceutical Industries Inc. (Sun) filed a similar ANDA for Gemzar. We are evaluating our option to bring legal action against Sun. We expect to prevail in litigation involving our Gemzar patents and believe that claims made by these generic companies that our patents are not valid are without merit. However, it is not possible to predict or determine the outcome of such litigation, and accordingly, we can provide no assurance that we will prevail. An unfavorable outcome could have a material adverse impact on our consolidated results of operations.

In March 2004, the office of the U.S. Attorney for the Eastern District of Pennsylvania advised us that it has commenced a civil investigation related to our U.S. marketing and promotional practices, including our communications with physicians and

remuneration of physician consultants and advisors, with respect to Zyprexa, Prozac®, and Prozac Weekly™. In October 2005, the U.S. Attorney's office advised that it is also conducting an inquiry regarding certain rebate agreements we entered into with a pharmacy benefit manager covering Axid®, Evista, Humalogâ, Humulinâ, Prozac, and Zyprexa. The inquiry includes a review of Lilly's Medicaid best price reporting related to the product sales covered by the rebate agreements. We are cooperating with the U.S. Attorney in these investigations, including providing a broad range of documents and information relating to the investigations. In June 2005, we received a subpoena from the office of the Attorney General, Medicaid Fraud Control Unit, of the State of Florida, seeking production of documents relating to sales of Zyprexa and our marketing and promotional practices with respect to Zyprexa. In September 2006, we received a subpoena from the California Attorney General's office seeking production of documents related to our efforts to obtain and maintain Zyprexa's status on California's formulary, marketing and promotional practices with respect to Zyprexa, and remuneration of health care providers. It is possible that other Lilly products could become subject to investigation and that the outcome of these matters could include criminal charges and fines, penalties, or other monetary or nonmonetary remedies. We cannot predict or determine the outcome of these matters or reasonably estimate the amount or range of amounts of any fines or penalties that might result from an adverse outcome. It is possible, however, that an adverse outcome could have a material adverse impact on our consolidated results of operations, liquidity, and financial position. We have implemented and continue to review and enhance a broadly based compliance program that includes comprehensive compliance-related activities designed to ensure that our marketing and promotional practices, physician communications, remuneration of health care professionals, managed care arrangements, and Medicaid best-price reporting comply with applicable laws and regulations.

We have been named as a defendant in a large number of Zyprexa product liability lawsuits in the United States and have been notified of many other claims of individuals who have not filed suit. The lawsuits and unfiled claims (together the "claims") allege a variety of injuries from the use of Zyprexa, with the majority alleging that the product caused or contributed to diabetes or high blood-glucose levels. The claims seek substantial compensatory and punitive damages and typically accuse us of inadequately testing for and warning about side effects of Zyprexa. Many of the claims also allege that we improperly promoted the drug. Almost all of the federal lawsuits are part of a Multi-District Litigation (MDL) proceeding before The Honorable Jack Weinstein in the Federal District Court for the Eastern District of New York (MDL No. 1596). The MDL includes three lawsuits requesting certification of class actions on behalf of those who allegedly suffered injuries from the administration of Zyprexa. We have entered into agreements with various plaintiffs' counsel halting the running of the statutes of limitation (tolling agreements) with respect to a number of claimants who do not have lawsuits on file.

Since June 2005, we have entered into agreements with various claimants' attorneys involved in U.S. Zyprexa product liability litigation to settle approximately 10,500 claims, including a large number of previously filed lawsuits (including the three purported class actions mentioned above), tolled claims, and other informally asserted claims. The settlements are being overseen and distributed by court-approved claims administrators.

The U.S. Zyprexa product liability claims not subject to these agreements include approximately 1,500 lawsuits in the U.S. covering approximately 9,700 claimants, and approximately 850 tolled claims. The first trials are scheduled for April 2007 in the Federal District Court for the Eastern District of New York. In addition, we have been served with a lawsuit seeking class certification in which the members of the purported class are seeking refunds and medical monitoring. Finally, in early 2005, we were served with four lawsuits seeking class-action status in Canada on behalf of patients who took Zyprexa. One of these four lawsuits has been certified for certain residents of Quebec. The allegations in the Canadian actions are similar to those in the litigation pending in the United States. We are prepared to continue our vigorous defense of Zyprexa in all remaining cases.

In December 2004, we were served with two lawsuits brought in state court in Louisiana on behalf of the Louisiana Department of Health and Hospitals, alleging that Zyprexa caused or contributed to diabetes or high blood-glucose levels, and that we improperly promoted the drug. These cases have been removed to federal court and are now part of the MDL proceedings in the Eastern District of New York. In these actions, the Department of Health and Hospitals seeks to recover the costs it paid for Zyprexa through Medicaid and other drug-benefit programs, as well as the costs the department alleges it has incurred and will incur to treat Zyprexa-related illnesses. In 2006, we were served with similar lawsuits filed by the states of Alaska, West Virginia, Mississippi, and New Mexico in the courts of the respective states.

In 2005, two lawsuits were filed in the Eastern District of New York purporting to be nationwide class actions on behalf of all consumers and third-party payors, excluding governmental entities, that have made or will make payments for their members or insured patients being prescribed Zyprexa. These actions have now been consolidated into a single lawsuit, which is brought under certain state consumer-protection statutes, the federal civil RICO statute, and common law theories, seeking a refund of the cost of Zyprexa, treble damages, punitive damages, and attorneys' fees. Four additional lawsuits were filed in 2006: two in the Eastern District of New York, one in the Southern District of Indiana, and one in Indiana state court, all on similar grounds. As with the product liability suits, these lawsuits allege that we inadequately tested for and warned about side effects of Zyprexa and improperly promoted the drug.

We have insurance coverage for a portion of our Zyprexa product liability claims exposure. The third-party insurance carriers have raised defenses to their liability under the policies and are seeking to rescind the policies. The dispute is now the subject of litigation

in the federal court in Indianapolis against certain carriers and in arbitration in Bermuda against other carriers. While we believe our position is meritorious, there can be no assurance that we will prevail.

In addition, we have been named as a defendant in numerous other product liability lawsuits involving primarily diethylstilbestrol (DES) and thimerosal.

With respect to the product liability claims currently asserted against us, we have accrued for our estimated exposures to the extent they are both probable and estimable based on the information available to us. In addition, we have accrued for certain product liability claims incurred but not filed to the extent we can formulate a reasonable estimate of their costs. We estimate these expenses based primarily on historical claims experience and data regarding product usage. Legal defense costs expected to be incurred in connection with significant product liability loss contingencies are accrued when probable and reasonably estimable. A portion of the costs associated with defending and disposing of these suits is covered by insurance. We record receivables for insurance-related recoveries when it is probable they will be realized. These receivables are classified as a reduction of the litigation charges on the statement of income. We estimate insurance recoverables based on existing deductibles, coverage limits, our assessment of any defenses to coverage that might be raised by the carriers, and the existing and projected future level of insolvencies among the insurance carriers.

In the second quarter of 2005, we recorded a net pre-tax charge of $1.07 billion for product liability matters. The $1.07 billion net charge takes into account our estimated recoveries from our insurance coverage related to these matters. The charge covers the following:

- The cost of the Zyprexa settlements described above; and,
- Reserves for product liability exposures and defense costs regarding currently known and expected claims to the extent we can formulate a reasonable estimate of the probable number and cost of the claims. A substantial majority of these exposures and costs relate to current and expected Zyprexa claims not included in the settlements. We have estimated these charges based primarily on historical claims experience, data regarding product usage, and our historical product liability defense cost experience.

During 2005, $700.0 million was paid in connection with Zyprexa settlements, while the cash related to other reserves for product liability exposures and defense costs is expected to be paid out over the next several years, including 2006. The timing of our insurance recoveries is uncertain.

We cannot predict with certainty the additional number of lawsuits and claims that may be asserted. In addition, although we believe it is probable, there can be no assurance that the Zyprexa settlements described above will be concluded. The ultimate resolution of Zyprexa product liability and related litigation could have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

Because of the nature of pharmaceutical products, it is possible that we could become subject to large numbers of product liability claims for other products in the future. We have experienced difficulties in obtaining product liability insurance due to a very restrictive insurance market, and therefore will be largely self-insured for future product liability losses. In addition, as noted above, there is no assurance that we will be able to fully collect from our insurance carriers on past claims.

In June 2002, we were sued by Ariad Pharmaceuticals, Inc., the Massachusetts Institute of Technology, the Whitehead Institute for Biomedical Research and the President and Fellows of Harvard College in the U.S. District Court for the District of Massachusetts alleging that sales of two of our products, Xigris® and Evista, were inducing the infringement of a patent related to the discovery of a natural cell signaling phenomenon in the human body and seeking royalties on past and future sales of these products. We believe that these allegations are without legal merit and that we will ultimately prevail on these issues. In June 2005, the United States Patent and Trademark Office commenced a re-examination of the patent in order to consider certain issues raised by us relating to the validity of the patent. A jury trial commenced in Boston on April 10, 2006 on the patent validity and infringement issues. On May 4, 2006, the jury issued an initial decision in the case that Xigris and Evista sales infringe the patent. The jury awarded the plaintiffs approximately $65 million in damages, calculated by applying a 2.3 percent royalty to all U.S. sales of Xigris and Evista from the date of issuance of the patent through the date of trial. We will seek to have the jury verdict overturned by the trial court judge, and if unsuccessful, will appeal the decision to the Court of Appeals for the Federal Circuit. In addition, a separate bench trial with the U.S. District Court of Massachusetts was held the week of August 7, 2006, on our contention that the patent is unenforceable and impermissibly covers natural processes. No decision has been rendered.

Also, under the Comprehensive Environmental Response, Compensation, and Liability Act, commonly known as Superfund, we have been designated as one of several potentially responsible parties with respect to fewer than 10 sites. Under Superfund, each responsible party may be jointly and severally liable for the entire amount of the cleanup. We also continue remediation of certain of our own sites. We have accrued for estimated Superfund cleanup costs, remediation, and certain other environmental matters. This

takes into account, as applicable, available information regarding site conditions, potential cleanup methods, estimated costs, and the extent to which other parties can be expected to contribute to payment of those costs. We have reached a settlement with our liability insurance carriers providing for coverage for certain environmental liabilities.

The litigation accruals and environmental liabilities and the related estimated insurance recoverables have been reflected on a gross basis as liabilities and assets, respectively, on our consolidated balance sheets.

While it is not possible to predict or determine the outcome of the patent, product liability, or other legal actions brought against us or the ultimate cost of environmental matters, we believe that, except as noted above, the resolution of all such matters will not have a material adverse effect on our consolidated financial position or liquidity, but could possibly be material to the consolidated results of operations in any one accounting period.

EARNINGS PER SHARE

Unless otherwise noted in the footnotes, all earnings per-share amounts are presented on a diluted basis; that is, based on the weighted-average number of outstanding common shares plus the effect of all potentially dilutive common shares (primarily unexercised stock options).

STOCK-BASED COMPENSATION

We adopted Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment (SFAS 123R), effective January 1, 2005. SFAS 123R requires the recognition of the fair value of stock-based compensation in net income. Stock-based compensation primarily consists of stock options and performance awards. We recognized pretax stock-based compensation cost in the amount of $83.0 million and $101.3 million in the third quarter of 2006 and 2005, respectively. In the first nine months of 2006 and 2005, we recognized stock-based compensation expense of $274.3 million and $309.5 million, respectively.

As of September 30, 2006, the total remaining unrecognized compensation cost related to nonvested stock options and performance awards amounted to $128.9 million and $51.2 million, respectively, which will be amortized over the weighted-average remaining requisite service periods, which are approximately 17 months and 3 months, respectively.

Under our policy, all stock option awards are approved prior to the date of grant and the exercise price is the average of the high and low market price on the date of grant. The Compensation Committee of the Board of Directors approves the value of the award and the date of grant. Options that are awarded as part of annual total compensation are made on specific grant dates scheduled in advance. With respect to option awards given to new hires, our policy requires approval of such awards prior to the grant date, and the options are granted on a predetermined monthly date immediately following the date of hire.

RETIREMENT BENEFITS

Net pension and retiree health benefit expense included the following components:

	Defined Benefit Pension Plans			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
	(Dollars in millions)			
Components of net periodic benefit cost				
Service cost	$ 67.8	$ 79.2	$ 206.1	$ 233.6
Interest cost	81.8	73.5	244.0	222.5
Expected return on plan assets	(121.2)	(111.8)	(361.5)	(334.8)
Amortization of prior service cost	1.4	1.9	4.3	5.8
Recognized actuarial loss	31.8	25.7	94.9	77.9
Net periodic benefit cost	$ 61.6	$ 68.5	$ 187.8	$ 205.0

	Retiree Health Benefit Plans			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
	(Dollars in millions)			
Components of net periodic benefit cost				
Service cost	$ 18.0	$ 14.7	$ 53.9	$ 44.1
Interest cost	24.4	20.0	73.3	60.1
Expected return on plan assets	(22.5)	(18.7)	(67.4)	(54.4)
Amortization of prior service cost	(3.9)	(3.9)	(11.6)	(11.9)
Recognized actuarial loss	27.0	21.5	80.9	64.6
Net periodic benefit cost	$ 43.0	$ 33.6	$129.1	$102.5

In 2006, we contributed approximately $30 million to our defined benefit pension plans to satisfy minimum funding requirements for the year. In addition, we contributed approximately $140 million of additional discretionary funding to our defined benefit plans and approximately $90 million of discretionary funding to our post retirement benefit plans. We do not expect to contribute additional amounts to our plans during the remainder of 2006.

OTHER INCOME — NET

Other income — net, was comprised of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
	(Dollars in millions)			
Interest expense	$ 62.7	$ 24.3	$ 193.5	$ 60.9
Interest income	(67.5)	(51.9)	(195.6)	(144.2)
Joint venture (income) loss	(23.8)	(5.8)	(66.1)	7.3
Other	(27.4)	(51.6)	(66.9)	(153.0)
	$(56.0)	$(85.0)	$(135.1)	$(229.0)

The joint venture (income) loss represents our share of the Lilly ICOS LLC joint venture results of operations, net of income taxes.

SHAREHOLDERS' EQUITY

As of September 30, 2006, we have purchased $2.58 billion of our previously announced $3.0 billion share repurchase program. During the nine months ended September 30, 2006, we acquired 2.1 million shares pursuant to this program. We do not expect any share repurchases during the remainder of 2006.

IMPLEMENTATION OF NEW FINANCIAL ACCOUNTING PRONOUNCEMENTS

In September 2006, the FASB issued Statement No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans — an amendment of FASB Statements No. 87, 88, 106, and 132(R). SFAS 158 requires the recognition of the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position, the measurement of a plan's assets and its obligations that determine its funded status as of the end of the employer's fiscal year, and the recognition of changes in that funded status in the year in which the changes occur through comprehensive income. Additional footnote disclosures will also be required. SFAS 158 is effective for us as of December 31, 2006 and is required to be adopted prospectively. Because the impact on our consolidated financial position upon adoption will depend on the facts and circumstances as of December 31, 2006, we cannot determine the impact at this time; however, if we would have adopted SFAS 158 as of December 31, 2005, there would have been a reduction to our net assets and shareholder's equity of approximately $1.7 billion. There will be no impact to our statements of income or cash flows. We do not expect the change in the measurement date to have an impact on our financial statements.

In September 2006, the SEC issued Staff Accounting Bulletin (SAB) No. 108, which provides interpretive guidance on how the effects of carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. The SEC staff believes that errors should be quantified using both a balance sheet and income statement approach and evaluated as to whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. The SEC staff has stated that it will not object if there is a one-time cumulative effect adjustment recorded to correct errors existing in prior years that previously had been considered immaterial — quantitatively and qualitatively - based on appropriate use of the registrant's previous approach. SAB 108 describes the circumstances where this would be appropriate as

well as the required disclosures and is effective for fiscal years ending after November 15, 2006; therefore we will be required to apply this Bulletin in the year ending December 31, 2006. We are currently evaluating SAB 108 and have not yet determined its impact; however, based on currently available information, we do not expect a material impact on our consolidated financial position or results of operations.

In June 2006, the FASB issued FIN 48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Interpretation is effective for fiscal years beginning after December 15, 2006; therefore, we will be required to adopt this Interpretation in the first quarter of 2007. We are currently evaluating FIN 48 and have not yet determined the impact the adoption of this Interpretation will have on our consolidated financial position or results of operations.

In the fourth quarter of 2005, we adopted Financial Accounting Standards Board (FASB) Interpretation (FIN) 47, Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143. FIN 47 requires us to record the fair value of a liability for conditional asset retirement obligations in the period in which it is incurred, which is adjusted to its present value each subsequent period. In addition, we are required to capitalize a corresponding amount by increasing the carrying amount of the related long-lived asset, which is depreciated over the useful life of the related long-lived asset. The adoption of FIN 47 on December 31, 2005, resulted in a cumulative effect of a change in accounting principle of $22.0 million, net of income taxes of $11.8 million.

POTENTIAL ASSET IMPAIRMENTS, RESTRUCTURING, AND OTHER SPECIAL CHARGES

As part of our ongoing efforts to maximize performance and efficiencies, including the streamlining of manufacturing operations and research and development activities, as announced in June 2006, we have been considering the future of three European facilities, which include the R&D facilities in Mont St. Guibert, Belgium and Hamburg, Germany, and the dry products manufacturing facility in Basingstoke, England. On October 16, 2006, the Board of Directors approved a plan to close the Hamburg, Germany, facility and also approved a social package, including severance payments that were negotiated with the site works council. Under the agreement, operations will decrease during the rest of 2006 and into the first half of 2007, with the official closing anticipated by mid-2007. This will result in a fourth-quarter charge to asset impairment, restructuring and other special charges of $40 million to $50 million (pretax), or $.02 to $.03 per share (after-tax), composed of $35 million to $40 million in severance related charges and lease termination costs, substantially all of which is expected to be in cash, and $5 million to $10 million in non-cash asset impairment charges. We have also been considering the closure of the Basingstoke plant as well as the sale of the plant as an ongoing operation. Several companies have expressed interest in potentially purchasing this site as an ongoing operation, and management intends to diligently pursue the sale option and make a decision by year end. If no viable sale option has been identified by that time, the Board has authorized management to proceed with the closure of the facility and implementation of a severance package negotiated with the employee representatives. No final decisions have been made with respect to the Basingstoke and Mont St. Guibert sites. However, severance and impairment charges as a result of any potential sale or site closure could be significant.

SUBSEQUENT EVENT

On October 17, 2006, we signed an agreement to acquire ICOS Corporation (ICOS) for approximately $2.1 billion in cash. The acquisition brings the full value of Cialis® to us and enables us to realize operational efficiencies in the further development, marketing and selling of this product. Consummation of the acquisition is subject to antitrust clearance under the Hart-Scott-Rodino Act, approval of the ICOS shareholders, and other customary closing conditions. Upon the closing of the transaction, which is expected in late 2006 or early 2007, we will incur a one-time charge to earnings for acquired in-process research and development (IPR&D), but it is premature to estimate what that charge will be.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

OPERATING RESULTS

Executive Overview

I. Financial Results

Our worldwide sales for the third quarter increased 7 percent to $3.86 billion. Net income was $873.6 million, or $.80 per share, for the third quarter of 2006 compared with $794.4 million, or $.73 per share, for the third quarter of 2005, representing an increase of 10 percent in both net income and earnings per share. The earnings growth was driven by sales increasing at a faster rate than cost of products sold and research and development expenses, offset partially by higher marketing and administrative expenses and decreased other income. Net income was $2.53 billion, or $2.33 per share, for the first nine months of 2006 compared with $1.28 billion, or $1.17 per share, for the first nine months of 2005. These amounts include the impact of the product liability litigation charge of $1.07 billion that was taken in the second quarter of 2005. In addition to this product liability charge, the earnings increase in the nine-month period was driven primarily by increased sales and decreased cost of sales, offset by decreased other income.

II. Business Development, and Recent Product and Late-Stage Pipeline Developments

- On October 17, 2006, we announced our acquisition of ICOS Corporation for approximately $2.1 billion in cash. The acquisition brings the full value of Cialis to us and enables us to realize operational efficiencies in the further development, marketing and selling of this product. We expect this acquisition will increase our earnings and earnings growth rate beginning in 2008 and, after a significant addition to sales in 2007, will modestly accelerate our sales growth rate thereafter. Upon the closing of the transaction, which is expected in late 2006 or early 2007, we will incur a one-time charge to earnings for acquired in-process research and development (IPR&D), but it is premature to estimate what that charge will be. In addition, we expect the impact of including the operations of ICOS in our financial results will be modestly dilutive to earnings in 2007. Consummation of the acquisition is subject to antitrust clearance under the Hart-Scott-Rodino Act, approval of the ICOS shareholders, and other customary closing conditions.
- We received an approvable letter from the U.S. Food and Drug Administration (FDA) for Arxxant™ for the treatment of diabetic retinopathy. The FDA has indicated that it will require efficacy data from an additional Phase III study before it will consider approving the molecule. We have decided to appeal the FDA's decision and have recently begun discussions with the agency. We reached this decision by considering the significance of the unmet medical need that diabetic retinopathy represents, the efficacy demonstrated in the completed clinical studies and the safety profile shown in more than 3,300 patient years of clinical trial exposure. There can be no assurance that our appeal will be successful.
- The Committee for Medicinal Products for Human Use of the European Medicines Evaluation Agency issued a positive opinion recommending approval of Byetta® for the treatment of type 2 diabetes. Marketing authorization by the European Commission is expected later this year. Byetta is already approved in the U.S. for this indication.
- We submitted data to the FDA for consideration of a new treatment-resistant depression (TRD) indication for Symbyax®, available as a range of fixed combinations of Zyprexa and Prozac, as well as for Zyprexa used in combination with Prozac. Symbyax is already approved in the U.S. for the treatment of bipolar depression.
- During the second quarter of 2006, Gemzar was approved in the U.S. for the treatment of recurrent ovarian cancer in combination with carboplatin.
- During the second quarter of 2006, we submitted a supplemental NDA to the FDA for Cymbaltaâ for the treatment of generalized anxiety disorder. We are also conducting Phase III studies on Cymbalta for the treatment of fibromyalgia, a chronic, often debilitating pain disorder.
- During the second quarter of 2006, we initiated a Phase III clinical trial to study enzastaurin as a maintenance therapy to prevent relapse in patients with diffuse large B-cell lymphoma. We initiated a Phase III clinical trial of enzastaurin, a targeted oral agent, during the first quarter of 2006, for the treatment of relapsed glioblastoma multiforme, an aggressive and malignant form of brain cancer.

III. Legal, Regulatory, and Other Matters

Certain generic manufacturers have challenged our U.S. compound patent for Zyprexa and are seeking permission to market generic versions of Zyprexa prior to its patent expiration in 2011. On April 14, 2005, the U.S. District Court in Indianapolis ruled in our favor on all counts, upholding our patents. The decision has been appealed.

We have reached agreements with claimants' attorneys involved in certain U.S. Zyprexa product liability litigation to settle a large number of claims against us relating to the medication. A large number of claims remain. As a result of our product liability exposures, the substantial majority of which were related to Zyprexa, we recorded a net pretax charge of $1.07 billion in the second quarter of 2005.

In March 2004, we were notified by the U.S. Attorney's office for the Eastern District of Pennsylvania that it has commenced a civil investigation relating to our U.S. sales, marketing, and promotional practices.

As previously disclosed, we have been considering the future of three European facilities, which include the R&D facilities in Mont St. Guibert, Belgium, and Hamburg, Germany, and the dry products manufacturing facility in Basingstoke, England. On October 16, 2006, the Board of Directors approved a plan to close the Hamburg, Germany, facility by June 30, 2007. No final decisions have been made with respect to the Basingstoke and Mont St. Guibert sites. However, severance and impairment charges as a result of any potential sale or site closure could be significant.

In the United States, implementation of the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (MMA), which provides a prescription drug benefit under the Medicare program, took effect January 1, 2006. In 2006, we are experiencing a one-time sales benefit as a result of MMA; however, in the long term there is additional risk of increased pricing pressures. While the MMA prohibits the Secretary of Health and Human Services (HHS) from directly negotiating prescription drug prices with manufacturers, we expect continued challenges to that prohibition over the next several years. Also, the MMA retains the authority of the Secretary of HHS to prohibit the importation of prescription drugs, but we expect Congress to consider several measures that could remove that authority and allow for the importation of products into the U.S. regardless of their safety or cost. If adopted, such legislation would likely have a negative effect on our U.S. sales. Recently, language allowing for personal importation of a 90-day supply of medication from Canada only was passed into law via the Homeland Security Appropriations bill. This language only allows for medication to be carried in person from Canada to the U.S. and does not authorize mail or Internet importation. Further, the language disallows certain medications including injectibles. We believe there is some chance that the new and expanded prescription drug coverage for seniors under the MMA will alleviate the perceived need for a federal importation scheme. Additionally, notwithstanding the federal law that continues to prohibit all but the very narrow drug importation detailed above, approximately a dozen states have implemented importation schemes for their citizens, usually involving a website that links patients to selected Canadian pharmacies. One state has such a program for its state employees.

As a result of the passage of the MMA, aged and disabled patients jointly eligible for Medicare and Medicaid began receiving their prescription drug benefits through the Medicare program, instead of Medicaid, on January 1, 2006. This may relieve some state budget pressures but is unlikely to result in reduced pricing pressures at the state level. A majority of states have implemented supplemental rebates and restricted formularies in their Medicaid programs, and these programs are expected to continue in the post-MMA environment. Moreover, under the 2005 federal Deficit Reduction Act, states will have greater flexibility to impose new cost-sharing requirements on Medicaid beneficiaries for non-preferred prescription drugs that will result in certain beneficiaries bearing more of the cost. Several states also are attempting to extend discounted Medicaid prices to non-Medicaid patients. As a result, we expect pressures on pharmaceutical pricing to continue.

As it relates to the new Medicare program, we announced in the second quarter of 2006 that we temporarily extended our U.S. patient assistance program, LillyAnswers. The temporary extension of LillyAnswers allows patients who are not enrolled in Medicare Part D access to the LillyAnswers program until December 31, 2006. We also temporarily extended LillyAnswers for patients who have enrolled in a Medicare Part D plan and need assistance for Zyprexa and Forteoâ. We have received a favorable opinion from the U.S. Department of Health and Human Services Office of the Inspector General (OIG) for our proposal for an "Outside Part D" patient assistance program (i.e., the LillyMedicareAnswers program) which will provide assistance for Zyprexa, Forteo, and Humatrope® beyond the end of this year to eligible patients enrolled in a Medicare Part D plan. We currently anticipate that the specific LillyAnswers program extension involving Zyprexa, Forteo, and Humatrope for patients enrolled in a Medicare Part D plan will continue to be available until December 31, 2006. In order to participate in either the temporary extension as described above or the new LillyMedicareAnswers program, certain eligibility and certification requirements must be met.

International operations also are generally subject to extensive price and market regulations, and there are many proposals for additional cost-containment measures, including proposals that would directly or indirectly impose additional price controls or reduce the value of our intellectual property protection.

Sales

Sales growth for the third quarter and first nine months of 2006 was 7 percent and 6 percent, respectively. The primary drivers for growth in the third quarter of 2006 were Cymbalta, Byetta, Forteo, Alimta® and Zyprexa. Sales in the U.S. increased by $178.3 million, or 9 percent for the third quarter of 2006, and $527.3 million, or 9 percent for the first nine months of 2006, compared with the same periods of 2005. The U.S. growth comparison for the nine-month period also benefited from an estimated $170 million of wholesaler destocking in the first nine months of 2005 as a result of restructuring our arrangements with our U.S. wholesalers in the first quarter of 2005. We experienced a one-time sales benefit resulting from a shift of certain low-income patients from Medicaid to Medicare and increased access to medical coverage by certain patients previously covered under our LillyAnswers program following the implementation of MMA in 2006. This contributed part of the increases in U.S. net effective sales prices of 11 percent and 9 percent for the third quarter and first nine months of 2006, respectively. Sales outside the U.S. increased $84.7 million, or 5 percent, and $152.2 million, or 3 percent, for the third quarter and first nine months of 2006, respectively. Worldwide sales volume and exchange rates both increased by 1 percent and selling prices increased by 5 percent in the third quarter of 2006. For the first nine months of 2006, worldwide sales volume and selling prices increased 4 percent and 3 percent, respectively, while exchange rates decreased 1 percent.

The following tables summarize our net sales activity for the three- and nine-month periods ended September 30, 2006 and 2005:

	Three Months Ended September 30, 2006			Three Months Ended September 30, 2005	Percent Change
Product	U.S.[1]	Outside U.S.	Total	Total	From 2005
			(Dollars in millions)		
Zyprexa	$ 519.0	$ 565.7	$1,084.7	$1,035.1	5
Gemzar	153.0	201.6	354.6	334.3	6
Cymbalta	306.5	42.1	348.6	182.8	91
Humalog	199.0	123.2	322.2	306.2	5
Evista	162.8	95.1	257.9	260.3	(1)
Humulin	96.7	133.3	230.0	250.9	(8)
Animal health products	98.0	118.2	216.2	215.7	0
Alimta	89.9	67.3	157.2	122.3	29
Forteo	104.2	44.9	149.1	102.6	45
Strattera®	112.3	14.1	126.4	140.9	(10)
Humatrope	49.3	52.3	101.6	100.2	1
Fluoxetine products	37.8	40.5	78.3	112.4	(30)
Actos®	34.7	42.3	77.0	64.3	20
ReoPro®	26.6	40.3	66.9	70.9	(6)
Byetta	62.1	—	62.1	10.6	NM
Anti-infectives	1.0	57.5	58.5	104.7	(44)
Cialis[2]	1.4	54.2	55.6	40.9	36
Xigris	22.7	19.4	42.1	45.5	(7)
Other pharmaceutical products	29.6	45.5	75.1	100.5	(25)
Total net sales	$2,106.6	$1,757.5	$3,864.1	$3,601.1	

Product	Nine Months Ended September 30, 2006 U.S.[1]	Outside U.S.	Total	Nine Months Ended September 30, 2005 Total	Percent Change From 2005
			(Dollars in millions)		
Zyprexa	$1,555.8	$1,651.3	$ 3,207.1	$ 3,170.1	1
Gemzar	452.7	584.2	1,036.9	981.9	6
Humalog	584.2	363.1	947.3	888.6	7
Cymbalta	782.3	110.0	892.3	450.9	98
Evista	486.9	288.1	775.0	770.8	1
Humulin	264.8	403.5	668.3	757.5	(12)
Animal health products	274.7	340.8	615.5	612.3	1
Alimta	255.5	184.9	440.4	327.4	35
Strattera	373.5	49.2	422.7	384.1	10
Forteo	292.4	129.8	422.2	271.3	56
Actos	237.0	121.7	358.7	338.0	6
Humatrope	149.6	156.6	306.2	313.6	(2)
Fluoxetine products	113.4	122.3	235.7	339.1	(30)
Anti-infectives	25.3	190.7	216.0	326.7	(34)
ReoPro	84.5	128.9	213.4	225.4	(5)
Cialis[2]	4.6	158.5	163.1	124.9	31
Byetta	150.0	—	150.0	14.0	NM
Xigris	75.7	65.1	140.8	162.8	(14)
Other pharmaceutical products	76.7	157.4	234.1	306.8	(24)
Total net sales	$6,239.6	$5,206.1	$11,445.7	$10,766.2	

NM — Not meaningful

1 U.S. sales include sales in Puerto Rico.

2 Cialis had worldwide third-quarter and nine-month sales of $245.6 million and $701.8 million, respectively, representing increases of 26 percent and 31 percent, respectively, compared with the same periods of 2005. The sales shown in the tables above represent results in the territories in which we market Cialis exclusively. The remaining sales relate to the joint-venture territories of Lilly ICOS LLC (North America, excluding Puerto Rico, and Europe). Our share of the joint-venture territory sales, net of expenses, is reported in other income — net in our consolidated condensed statements of income.

Product Highlights

Zyprexa sales in the U.S. increased 3 percent in the third quarter and decreased 1 percent in first nine months of 2006, respectively, compared with the same periods of 2005. The increase resulted from an increase in prices, partially offset by lower demand. However, U.S. prescription volume has held steady during the first nine months of 2006. The increase in net effective selling prices was partially due to the transition of certain low-income patients from Medicaid to Medicare. Sales outside the U.S. increased 6 percent in the third quarter of 2006, driven by increased demand as well as the favorable impact of exchange rates, offset partially by lower prices. International sales for the first nine months of 2006 increased 3 percent, which was due to increased demand.

Diabetes care products, composed primarily of Humalog, Humulin, Actos, and Byetta, had worldwide net sales of $712.4 million and $2.18 billion in the third quarter and first nine months of 2006, respectively, representing increases of 9 percent and 6 percent compared with the same periods last year. Diabetes care revenues in the U.S. increased 14 percent and 10 percent, to $408.6 million and $1.28 billion for the third quarter and first nine months of 2006, respectively. These increases were primarily driven by sales of Byetta for both periods. Diabetes care revenues outside the U.S. increased 3 percent and 1 percent, to $303.8 million and $900.8 million in the third quarter and first nine months of 2006, respectively. Results from our primary diabetes care products are as follows:

- Humalog sales in the U.S. increased 3 percent and 6 percent during the third quarter and first nine months of 2006, respectively, due to higher prices, which were partially offset by a decline in demand. Humalog sales outside the U.S. increased 10 percent during the third quarter primarily due to increased demand, as well as a favorable impact of exchange rates, offset partially by lower prices. Humalog sales outside the U.S. increased 8 percent for the first nine months of 2006, primarily due to increased demand, offset by the unfavorable impact of exchange rates.
- Humulin sales decreased 10 percent and 16 percent in the U.S. for the third quarter and first nine months of 2006, respectively, driven primarily by the decline in demand due to continued competitive pressures, offset partially by higher prices. Humulin sales outside the U.S. decreased 7 and 9 percent during the third quarter and first nine months of 2006, respectively, due to a decline in demand.
- Actos revenues in the U.S., the majority of which represent service revenues from a copromotion agreement in the U.S. with Takeda Pharmaceuticals North America (Takeda), increased 17 percent and decreased 1 percent in the third quarter and first nine months of 2006, respectively. Actos is manufactured by Takeda Chemical Industries, Ltd., and sold in the U.S. by Takeda. As previously disclosed, since our share of revenue from the agreement with Takeda will not necessarily track with product sales, it is difficult to make quarterly comparisons for Actos revenue. Our U.S. marketing rights with respect to Actos expired in September 2006; however, we will continue receiving royalties from Takeda at a declining rate through September 2009. The arrangement outside the U.S. continues.
- Sales of Byetta, a first-in-class treatment for type 2 diabetes we market with Amylin Pharmaceuticals (Amylin), launched in the U.S. in June 2005, were $126.4 million and $293.2 million during the third quarter and first nine months of 2006, respectively. We report as revenue our 50 percent share of Byetta's gross margins and our sales of Byetta pen delivery devices to Amylin.

Gemzar sales increased 2 percent and 5 percent in the U.S. for the third quarter and first nine months of 2006, respectively, as compared to the same periods in 2005. This increase is attributable to higher prices in both periods, offset partially by lower demand in the third quarter due to competitive pressures. Gemzar sales outside the U.S. increased 9 percent and 6 percent for the third quarter and first nine months of 2006, respectively, which was due to increased demand, offset partially by lower prices. The third quarter also benefited from the favorable impact of exchange rates.

U.S. sales of Cymbalta, a treatment of major depressive disorder and diabetic peripheral neuropathic pain, increased 80 percent and 85 percent for the third quarter and first nine months of 2006, respectively, as compared to the same periods last year, due to strong demand. Cymbalta sales outside the U.S. continue to reflect significant growth due to recent international launches.

Evista sales in the U.S. increased 1 percent for both the third quarter and first nine months of 2006, as compared to the same periods in 2005, due to higher prices, offset by a decline in demand. Evista sales outside the U.S. decreased 4 percent and remained flat in the third quarter and nine month periods of 2006, due primarily to lower prices in both periods, offset by an increase in demand during the first nine months of 2006.

Alimta, a treatment of malignant pleural mesothelioma and second-line treatment of non-small-cell lung cancer, generated an increase in U.S. sales of 17 percent and 22 percent for the third quarter and first nine months of 2006, respectively, as compared to the same periods in 2005. Alimta sales outside the U.S. increased 48 percent and 57 percent during the third quarter and first nine months of 2006, respectively. These increases are attributable to growth in U.S. and international demand.

Forteo, a treatment for severe osteoporosis, increased 48 and 59 percent in the U.S. in the third quarter and first nine months of 2006, respectively, as compared to the same periods in 2005. In addition to increased demand, U.S. sales significantly benefited from access to medical coverage through the Medicare Part D program and from decreased utilization of our U.S. patient assistance program, LillyAnswers. Sales outside the U.S. increased 39 percent and 48 percent for the third quarter and first nine months of 2006, respectively, which was driven by increased demand along with a favorable impact in exchange rates during the third quarter, offset by a decrease in prices.

U.S. sales of Strattera, a treatment of attention-deficit hyperactivity disorder (ADHD) in children, adolescents, and adults, decreased 10 percent during the third quarter and increased 7 percent for the first nine months of 2006, compared with the same periods in 2005. The decline in sales in the third quarter was attributable to a decline in demand, offset by an increase in prices. The increase for the first nine months of 2006 was the result of higher prices as well as the reductions in the U.S. wholesaler inventory levels in 2005, offset by decline in demand.

Total worldwide product sales of Cialis in the third quarter and first nine months of 2006 were composed of $55.0 million and $161.2 million of sales in our territories, respectively, which are reported in our net sales, and $190.6 million and $540.5 million of sales in the joint-venture territories. Within the joint-venture territories, the U.S. sales of Cialis were $94.9 million and $271.3 million in the third quarter and first nine months of 2006, respectively, representing increases of 23 percent and 42 percent from the same periods of 2005. Cialis sales in our territories are reported in revenue, while our 50 percent share of the joint-venture net income is reported in other income — net. Cialis sales growth reflects both gains in market share and growth of the erectile dysfunction market during the third quarter and first nine months of 2006.

Gross Margin, Costs, and Expenses

For the third quarter of 2006, gross margins improved 1.2 percentage points, to 77.7 percent of net sales, compared with the third quarter of 2005. For the first nine months of 2006, gross margins increased 1.8 percentage points, to 77.9 percent of net sales, compared with the first nine months of 2005. The increase for the quarter was primarily due to increased product prices and increased production volume, partially offset by higher manufacturing expenses. This increase for the nine-month period was primarily due to favorable product prices and the favorable impact of foreign exchange rates, partially offset by higher manufacturing expenses.

Operating expenses (the aggregate of research and development and marketing and administrative expenses) increased 7 percent and 6 percent for the third quarter and first nine months of 2006, respectively, compared with the same periods of 2005. Investment in research and development increased 1 percent, to $755.7 million, and 3 percent, to $2.27 billion, for the third quarter and first nine months of 2006, respectively, and represent 20 percent of sales in both periods. Marketing and administrative expenses increased 12 percent, to $1.20 billion, and 8 percent, to $3.58 billion, for the third quarter and first nine months of 2006, respectively, driven largely by increased marketing expenses in support of key products, primarily Cymbalta.

Other income — net consists of interest expense, interest income, the after-tax operating results of the Lilly ICOS joint venture, and all other income and expense items.

- Interest expense for the third quarter and nine-month period in 2006 increased $38.4 million, to $62.7 million, and $132.6 million to $193.5 million, respectively, as compared to the same periods in 2005. These increases are a result of higher interest rates and less capitalized interest due to the completion in late 2005 of certain manufacturing facilities.
- Interest income increased $15.6 million, to $67.5 million and $51.4 million to $195.6 million for the third quarter and first nine months of 2006, respectively, as compared to the same periods in 2005, due to higher short-term interest rates.
- The Lilly ICOS joint-venture income was $23.8 million in the third quarter of 2006, compared with $5.8 million in the third quarter of 2005. For the first nine months of 2006, income was $66.1 million, compared with a loss of $7.3 million in the first nine months of 2005. The increase in both periods was due to increased Cialis sales and decreased selling and marketing expenses.
- Net other income and expense items decreased $24.2 million to $27.4 million for third-quarter 2006 and decreased $86.1 million to $66.9 million for the first nine months of 2006, as compared to the same periods in 2005. The decreases are largely a result of less income from business development transactions.

We incurred tax expense of $232.2 million and $672.6 million, for the third quarter and first nine months of 2006, respectively, representing an effective tax rate of 21 percent in both periods. Tax expense for the third quarter of 2005 was $224.1 million, representing an effective tax rate of 22 percent. Year-to-date comparisons to prior year are not meaningful due to the net loss before income taxes experienced in the second quarter of 2005.

FINANCIAL CONDITION

As of September 30, 2006, cash, cash equivalents, and short-term investments totaled $3.62 billion compared with $5.04 billion at December 31, 2005. Cash flow from operations of $2.12 billion was more than offset by net repayments of long-term debt of $1.60 billion, dividends paid of $1.30 billion and net capital expenditures of $667.8 million. Total debt at September 30, 2006, was $4.89 billion, a decrease of $1.61 billion as compared to December 31, 2005. We currently expect to repay additional debt of approximately $500 million by the end of 2006. We also intend to incur approximately $2.4 billion of debt to finance the ICOS acquisition at the time the transaction is completed.

We believe that cash generated from operations, along with available cash and cash equivalents, will be sufficient to fund our normal operating needs, including debt service, capital expenditures, dividends, and taxes for the remainder of 2006. We believe that amounts available through our existing commercial paper program should be adequate to fund maturities of short-term borrowings, if necessary. Various risks and uncertainties, including those discussed in the Financial Expectations for 2006 section, may affect our operating results and cash generated from operations.

LEGAL AND REGULATORY MATTERS

We are engaged in the following patent litigation matters brought pursuant to procedures set out in the Hatch-Waxman Act (the Drug Price Competition and Patent Term Restoration Act of 1984):

- Dr. Reddy's Laboratories, Ltd. (Reddy), Teva Pharmaceuticals, and Zenith Goldline Pharmaceuticals, Inc., which was subsequently acquired by Teva Pharmaceuticals (together, Teva), each submitted abbreviated new drug applications (ANDAs) seeking permission to market generic versions of Zyprexa prior to the expiration of our relevant U.S. patent (expiring in 2011) and alleging that this patent was invalid or not enforceable. We filed lawsuits against these companies in the U.S. District Court for the Southern District of Indiana, seeking a ruling that the patent is valid, enforceable, and being infringed. The district court ruled in our favor on all counts on April 14, 2005. We are now awaiting a decision by the Court of Appeals for the Federal Circuit, which on April 6, 2006, heard Reddy's and Teva's respective appeals of this ruling. We are confident Reddy's and Teva's claims are without merit and we expect to prevail. However, it is not possible to predict or determine the outcome of this litigation, and accordingly, we can provide no assurance that we will prevail on appeal. An unfavorable outcome would have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

- Barr Laboratories, Inc. (Barr), submitted an ANDA in 2002 seeking permission to market a generic version of Evista prior to the expiration of our relevant U.S. patents (expiring in 2012-2017) and alleging that these patents are invalid, not enforceable, or not infringed. In November 2002, we filed a lawsuit against Barr in the U.S. District Court for the Southern District of Indiana, seeking a ruling that these patents are valid, enforceable, and being infringed by Barr. Teva has also submitted an ANDA seeking permission to market a generic version of Evista. In June 2006, we filed a lawsuit against Teva in the U.S. District Court for the Southern District of Indiana, seeking a ruling that our relevant U.S. patents (expiring in 2012-2014) are valid, enforceable, and being infringed by Teva. No trial date has been set in either case. We believe Barr's and Teva's claims are without merit and we expect to prevail. However, it is not possible to predict or determine the outcome of this litigation, and accordingly, we can provide no assurance that we will prevail. An unfavorable outcome could have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

- Sicor Pharmaceuticals, Inc. (Sicor), a subsidiary of Teva, submitted ANDAs in November 2005 seeking permission to market generic versions of Gemzar® prior to the expiration of our relevant U.S. patents (expiring in 2010 and 2013), and alleging that these patents are invalid. In February 2006, we filed a lawsuit against Sicor in the U.S. District Court for the Southern District of Indiana, seeking a ruling that these patents are valid and are being infringed by Sicor. In response to our lawsuit, Sicor filed a declaratory judgment action in the U.S. District Court for the Central District of California. The California action has since been dismissed. In September 2006, we received notice that Mayne Pharma (USA) Inc. (Mayne) filed a similar ANDA for Gemzar. In October 2006, we filed a lawsuit against Mayne in the Southern District of Indiana in response to the ANDA filing. We are awaiting the filing of an answer to our complaint against Mayne. In October 2006, we received notice that Sun Pharmaceutical Industries Inc. (Sun) filed a similar ANDA for Gemzar. We are evaluating our option to bring legal action against Sun. We expect to prevail in litigation involving our Gemzar patents and believe that claims made by these generic companies that our patents are not valid are without merit. However, it is not possible to predict or determine the outcome of such litigation, and accordingly, we can provide no assurance that we will prevail. An unfavorable outcome could have a material adverse impact on our consolidated results of operations.

In March 2004, the office of the U.S. Attorney for the Eastern District of Pennsylvania advised us that it has commenced a civil investigation related to our U.S. marketing and promotional practices, including our communications with physicians and remuneration of physician consultants and advisors, with respect to Zyprexa, Prozac, and Prozac Weekly. In October 2005, the U.S. Attorney's office advised that it is also conducting an inquiry regarding certain rebate agreements we entered into with a pharmacy benefit manager covering Axid, Evista, Humalog, Humulin, Prozac, and Zyprexa. The inquiry includes a review of Lilly's Medicaid best price reporting related to the product sales covered by the rebate agreements. We are cooperating with the U.S. Attorney in these investigations, including providing a broad range of documents and information relating to the investigations. In June 2005, we received a subpoena from the office of the Attorney General, Medicaid Fraud Control Unit, of the State of Florida, seeking production of documents relating to sales of Zyprexa and our marketing and promotional practices with respect to Zyprexa. In September 2006, we received a subpoena from the California Attorney General's office seeking production of documents related to our efforts to obtain and maintain Zyprexa's status on California's formulary, marketing and promotional practices with respect to Zyprexa, and remuneration of health care providers. It is possible that other Lilly products could become subject to investigation and that the

outcome of these matters could include criminal charges and fines, penalties, or other monetary or nonmonetary remedies. We cannot predict or determine the outcome of these matters or reasonably estimate the amount or range of amounts of any fines or penalties that might result from an adverse outcome. It is possible, however, that an adverse outcome could have a material adverse impact on our consolidated results of operations, liquidity, and financial position. We have implemented and continue to review and enhance a broadly based compliance program that includes comprehensive compliance-related activities designed to ensure that our marketing and promotional practices, physician communications, remuneration of health care professionals, managed care arrangements, and Medicaid best-price reporting comply with applicable laws and regulations.

We have been named as a defendant in a large number of Zyprexa product liability lawsuits in the United States and have been notified of many other claims of individuals who have not filed suit. The lawsuits and unfiled claims (together the "claims") allege a variety of injuries from the use of Zyprexa, with the majority alleging that the product caused or contributed to diabetes or high blood-glucose levels. The claims seek substantial compensatory and punitive damages and typically accuse us of inadequately testing for and warning about side effects of Zyprexa. Many of the claims also allege that we improperly promoted the drug. Almost all of the federal lawsuits are part of a Multi-District Litigation (MDL) proceeding before The Honorable Jack Weinstein in the Federal District Court for the Eastern District of New York (MDL No. 1596). The MDL includes three lawsuits requesting certification of class actions on behalf of those who allegedly suffered injuries from the administration of Zyprexa. We have entered into agreements with various plaintiffs' counsel halting the running of the statutes of limitation (tolling agreements) with respect to a number of claimants who do not have lawsuits on file.

Since June 2005, we have entered into agreements with various claimants' attorneys involved in U.S. Zyprexa product liability litigation to settle approximately 10,500 claims, including a large number of previously filed lawsuits (including the three purported class actions mentioned above), tolled claims, and other informally asserted claims. The settlements are being overseen and distributed by court-approved claims administrators.

The U.S. Zyprexa product liability claims not subject to these agreements include approximately 1,500 lawsuits in the U.S. covering approximately 9,700 claimants, and approximately 850 tolled claims. The first trials are scheduled for April 2007 in the Federal District Court for the Eastern District of New York. In addition, we have been served with a lawsuit seeking class certification in which the members of the purported class are seeking refunds and medical monitoring. Finally, in early 2005, we were served with four lawsuits seeking class-action status in Canada on behalf of patients who took Zyprexa. One of these four lawsuits has been certified for certain residents of Quebec. The allegations in the Canadian actions are similar to those in the litigation pending in the United States. We are prepared to continue our vigorous defense of Zyprexa in all remaining cases.

In December 2004, we were served with two lawsuits brought in state court in Louisiana on behalf of the Louisiana Department of Health and Hospitals, alleging that Zyprexa caused or contributed to diabetes or high blood-glucose levels, and that we improperly promoted the drug. These cases have been removed to federal court and are now part of the MDL proceedings in the Eastern District of New York. In these actions, the Department of Health and Hospitals seeks to recover the costs it paid for Zyprexa through Medicaid and other drug-benefit programs, as well as the costs the department alleges it has incurred and will incur to treat Zyprexa-related illnesses. In 2006, we were served with similar lawsuits filed by the states of Alaska, West Virginia, Mississippi, and New Mexico in the courts of the respective states.

In 2005, two lawsuits were filed in the Eastern District of New York purporting to be nationwide class actions on behalf of all consumers and third-party payors, excluding governmental entities, that have made or will make payments for their members or insured patients being prescribed Zyprexa. These actions have now been consolidated into a single lawsuit, which is brought under certain state consumer-protection statutes, the federal civil RICO statute, and common law theories, seeking a refund of the cost of Zyprexa, treble damages, punitive damages, and attorneys' fees. Four additional lawsuits were filed in 2006: two in the Eastern District of New York, one in the Southern District of Indiana, and one in Indiana state court, all on similar grounds. As with the product liability suits, these lawsuits allege that we inadequately tested for and warned about side effects of Zyprexa and improperly promoted the drug.

We have insurance coverage for a portion of our Zyprexa product liability claims exposure. The third-party insurance carriers have raised defenses to their liability under the policies and are seeking to rescind the policies. The dispute is now the subject of litigation in the federal court in Indianapolis against certain carriers and in arbitration in Bermuda against other carriers. While we believe our position is meritorious, there can be no assurance that we will prevail.

In addition, we have been named as a defendant in numerous other product liability lawsuits involving primarily diethylstilbestrol (DES) and thimerosal.

With respect to the product liability claims currently asserted against us, we have accrued for our estimated exposures to the extent they are both probable and estimable based on the information available to us. In addition, we have accrued for certain product liability claims incurred but not filed to the extent we can formulate a reasonable estimate of their costs. We estimate these expenses based primarily on historical claims experience and data regarding product usage. Legal defense costs expected to be incurred in

connection with significant product liability loss contingencies are accrued when probable and reasonably estimable. A portion of the costs associated with defending and disposing of these suits is covered by insurance. We record receivables for insurance-related recoveries when it is probable they will be realized. These receivables are classified as a reduction of the litigation charges on the statement of income. We estimate insurance recoverables based on existing deductibles, coverage limits, our assessment of any defenses to coverage that might be raised by the carriers, and the existing and projected future level of insolvencies among the insurance carriers.

In the second quarter of 2005, we recorded a net pre-tax charge of $1.07 billion for product liability matters. The $1.07 billion net charge takes into account our estimated recoveries from our insurance coverage related to these matters. The charge covers the following:

- The cost of the Zyprexa settlements described above; and,
- Reserves for product liability exposures and defense costs regarding currently known and expected claims to the extent we can formulate a reasonable estimate of the probable number and cost of the claims. A substantial majority of these exposures and costs relate to current and expected Zyprexa claims not included in the settlements. We have estimated these charges based primarily on historical claims experience, data regarding product usage, and our historical product liability defense cost experience.

During 2005, $700.0 million was paid in connection with Zyprexa settlements, while the cash related to other reserves for product liability exposures and defense costs is expected to be paid out over the next several years, including 2006. The timing of our insurance recoveries is uncertain.

We cannot predict with certainty the additional number of lawsuits and claims that may be asserted. In addition, although we believe it is probable, there can be no assurance that the Zyprexa settlements described above will be concluded. The ultimate resolution of Zyprexa product liability and related litigation could have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

Because of the nature of pharmaceutical products, it is possible that we could become subject to large numbers of product liability claims for other products in the future. We have experienced difficulties in obtaining product liability insurance due to a very restrictive insurance market, and therefore will be largely self-insured for future product liability losses. In addition, as noted above, there is no assurance that we will be able to fully collect from our insurance carriers on past claims.

In June 2002, we were sued by Ariad Pharmaceuticals, Inc., the Massachusetts Institute of Technology, the Whitehead Institute for Biomedical Research and the President and Fellows of Harvard College in the U.S. District Court for the District of Massachusetts alleging that sales of two of our products, Xigris® and Evista, were inducing the infringement of a patent related to the discovery of a natural cell signaling phenomenon in the human body and seeking royalties on past and future sales of these products. We believe that these allegations are without legal merit and that we will ultimately prevail on these issues. In June 2005, the United States Patent and Trademark Office commenced a re-examination of the patent in order to consider certain issues raised by us relating to the validity of the patent. A jury trial commenced in Boston on April 10, 2006 on the patent validity and infringement issues. On May 4, 2006, the jury issued an initial decision in the case that Xigris and Evista sales infringe the patent. The jury awarded the plaintiffs approximately $65 million in damages, calculated by applying a 2.3 percent royalty to all U.S. sales of Xigris and Evista from the date of issuance of the patent through the date of trial. We will seek to have the jury verdict overturned by the trial court judge, and if unsuccessful, will appeal the decision to the Court of Appeals for the Federal Circuit. In addition, a separate bench trial with the U.S. District Court of Massachusetts was held the week of August 7, 2006, on our contention that the patent is unenforceable and impermissibly covers natural processes. No decision has been rendered.

Also, under the Comprehensive Environmental Response, Compensation, and Liability Act, commonly known as Superfund, we have been designated as one of several potentially responsible parties with respect to fewer than 10 sites. Under Superfund, each responsible party may be jointly and severally liable for the entire amount of the cleanup. We also continue remediation of certain of our own sites. We have accrued for estimated Superfund cleanup costs, remediation, and certain other environmental matters. This takes into account, as applicable, available information regarding site conditions, potential cleanup methods, estimated costs, and the extent to which other parties can be expected to contribute to payment of those costs. We have reached a settlement with our liability insurance carriers providing for coverage for certain environmental liabilities.

The litigation accruals and environmental liabilities and the related estimated insurance recoverables have been reflected on a gross basis as liabilities and assets, respectively, on our consolidated balance sheets.

While it is not possible to predict or determine the outcome of the patent, product liability, or other legal actions brought against us or the ultimate cost of environmental matters, we believe that, except as noted above, the resolution of all such matters will not have a

material adverse effect on our consolidated financial position or liquidity, but could possibly be material to the consolidated results of operations in any one accounting period.

FINANCIAL EXPECTATIONS FOR 2006

For the full year of 2006, we expect earnings per share to be in the range of $3.07 to $3.18. This guidance reflects the closure of the Hamburg, Germany research and development facility previously discussed, which will result in a fourth-quarter charge to asset impairment, restructuring and other special charges of $40 million to $50 million (pretax), or $.02 to $.03 per share (after tax). It does not, however, reflect any other future material unusual items, such as the impact of the ICOS acquisition, including the IPR&D charge, if the transaction closes in 2006. Nor does it include any charges that may occur if further decisions are reached related to our other two European sites.

We expect full-year 2006 sales to grow at approximately the low end of 7 percent to 9 percent growth range. In addition, we expect gross margins as a percent of sales to improve, operating expenses to grow in the mid-single digits in the aggregate, and other income — net, to contribute approximately $175 million to $250 million. Excluding the tax associated with the potential charges discussed above, we also anticipate the effective tax rate to be approximately 21 percent. In terms of cash flow, we expect capital expenditures to be at approximately $1.2 billion in 2006.

We caution investors that any forward-looking statements or projections made by us, including those above, are based on management's belief at the time they are made. However, they are subject to risks and uncertainties. Actual results could differ materially and will depend on, among other things, the continuing growth of our currently marketed products; developments with competitive products; the timing and scope of regulatory approvals and the success of our new product launches; asset impairments, restructurings, and acquisitions of compounds under development resulting in acquired in-process research and development charges; foreign exchange rates; wholesaler inventory changes; the outcome of the Zyprexa patent appeal; other regulatory developments, government investigations, patent disputes, and litigation; and the impact of governmental actions regarding pricing, importation, and reimbursement for pharmaceuticals. Other factors that may affect our operations and prospects are discussed in Item 1A of our 2005 Form 10-K, "Risk Factors." We undertake no duty to update these forward-looking statements.

AVAILABLE INFORMATION ON OUR WEBSITE

We make available through our company website, free of charge, our company filings with the Securities and Exchange Commission (SEC) as soon as reasonably practicable after we electronically file them with or furnish them to the SEC. The reports we make available include annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements, registration statements, and any amendments to those documents.

The website link to our SEC filings is http://investor.lilly.com/edgar.cfm.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures. Under applicable SEC regulations, management of a reporting company, with the participation of the principal executive officer and principal financial officer, must periodically evaluate the company's "disclosure controls and procedures," which are defined generally as controls and other procedures of a reporting company designed to ensure that information required to be disclosed by the reporting company in its periodic reports filed with the commission (such as this Form 10-Q) is recorded, processed, summarized, and reported on a timely basis.

Our management, with the participation of Sidney Taurel, chairman and chief executive officer, and Derica W. Rice, senior vice president and chief financial officer, evaluated our disclosure controls and procedures as of September 30, 2006, and concluded that they are effective.

(b) Changes in Internal Controls. During the third quarter of 2006, there were no changes in our internal control over financial reporting that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

See Part I, Item 2, Management's Discussion and Analysis, "Legal and Regulatory Matters," for information on various legal proceedings, including but not limited to:

- The U.S. patent litigation involving Zyprexa, Evista, and Gemzar

- The civil investigation by the U.S. Attorney for the Eastern District of Pennsylvania relating to our U.S. sales, marketing, and promotional practices
- The Zyprexa product liability and related litigation, including claims brought on behalf of healthcare payors
- The legal proceedings we have filed against several of our product liability insurance carriers with respect to our coverage for the Zyprexa product liability claims

That information is incorporated into this Item by reference.

Other Product Liability Litigation

We refer to Part I, Item 3, of our Form 10-K annual report for 2005 for the discussion of product liability litigation involving diethylstilbestrol (DES) and vaccines containing the preservative thimerosal. In the DES litigation, we have been named as a defendant in approximately 70 suits involving approximately 120 claimants. In the thimerosal litigation, we have been named as a defendant in approximately 360 suits with approximately 975 claimants.

While it is not possible to predict or determine the outcome of the patent, product liability, or other legal actions brought against us or the ultimate cost of environmental matters, we believe that, except as noted above, the resolution of all such matters will not have a material adverse effect on our consolidated financial position or liquidity but could possibly be material to the consolidated results of operations in any one accounting period.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table summarizes the activity related to repurchases of our equity securities during the quarter ended September 30, 2006:

Period	Total Number of Shares Purchased (a)	Average Price Paid per Share (b)	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (c)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (d)
	(in thousands)			(Dollars in millions)
July 2006	4	$55.66	—	$419.2
August 2006	16	53.75	—	419.2
September 2006	24	55.86	—	419.2
Total	44		—	

The amounts presented in columns (a) and (b) above represent purchases of common stock related to employee stock option exercises. The amounts presented in columns (c) and (d) in the above table represent activity related to our $3.0 billion share repurchase program announced in March 2000. As of September 30, 2006, we have purchased $2.58 billion related to this program. During the third quarter of 2006, no shares were repurchased pursuant to this program and we do not expect to purchase any shares under this program during the remainder of 2006.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits. The following documents are filed as exhibits to this Report:

EXHIBIT 10.1	The Eli Lilly and Company Bonus Plan, as amended
EXHIBIT 10.2	2007 Change In Control Severance Pay Plan for Select Employees, as amended
EXHIBIT 10.3	Agreement and Plan of Merger by and among Eli Lilly and Company, Tour Merger Sub, Inc., and ICOS Corporation, which is incorporated by reference from Exhibit 2.1 to the Form 8-K filed by ICOS Corporation on October 17, 2006
EXHIBIT 11.	Statement re: Computation of Earnings (Loss) per Share
EXHIBIT 12.	Statement re: Computation of Ratio of Earnings From Continuing Operations to Fixed Charges

EXHIBIT 31.1	Rule 13a-14(a) Certification of Sidney Taurel, Chairman of the Board and Chief Executive Officer
EXHIBIT 31.2	Rule 13a-14(a) Certification of Derica W. Rice, Senior Vice President and Chief Financial Officer
EXHIBIT 32.	Section 1350 Certification

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

ELI LILLY AND COMPANY
(Registrant)

Date November 1, 2006

/s/James B. Lootens
James B. Lootens
Secretary and Deputy General Counsel

Date November 1, 2006

/s/Arnold C. Hanish
Arnold C. Hanish
Executive Director, Finance, and
Chief Accounting Officer

INDEX TO EXHIBITS

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EXHIBIT 10.1

The Eli Lilly and Company Bonus Plan

(as amended October 16, 2006)

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The Eli Lilly and Company Bonus Plan
(as amended October 16, 2006)

SECTION 1. PURPOSE

The purpose of The Eli Lilly and Company Bonus Plan is to encourage and promote eligible employees to create and deliver innovative pharmaceutical-based health care solutions that enable people to live longer, healthier and more active lives, to outgrow our competitors through a constant stream of pharmaceutical innovation, and to materially increase shareholder value. The Plan is designed to accomplish the following key objectives:

a. motivate superior employee performance through the implementation of a performance-based bonus system for all eligible management employees, United States employees (including those in Puerto Rico) and other employees as may be designated from time to time;

b. encourage eligible employees to take greater ownership of the company and provide "Answers that Matter" daily by creating a direct relationship between key company measurements and individual bonus payouts; and

c. enable the Company to attract and retain employees that will be instrumental in driving sustained growth and performance of Eli Lilly and Company by providing a competitive bonus program that rewards outstanding performance consistent with the Company's mission, values and increased shareholder value.

The Plan is intended to satisfy the requirements for providing "performance-based" compensation under Section 162(m) of the Internal Revenue Code.

SECTION 2. DEFINITIONS

The following words and phrases as used in this Plan will have the following meanings unless a different meaning is clearly required by the context. Masculine pronouns will refer both to males and to females:

2.1 Applicable Year means the calendar year immediately preceding the year in which payment of the Company Bonus is payable pursuant to Section 6. For example, the Applicable Year for 2005 payout is January 1, 2004 through December 31, 2004.

2.2 Bonus Target means the percentage of Participant Earnings for each Participant as described in Section 5.6(a) below.

2.3 Committee means (i) with respect to the Executive Officers of Lilly, the Compensation Committee, the members of which will be selected by the Board of Directors of Lilly,

from among its members; and (ii) with respect to all other Eligible Employees, the Compensation Committee of the Board of Directors or its designee. Each member of the Compensation Committee will, to the extent deemed necessary or appropriate by the Board of Directors, satisfy the requirements of an "outside director" within the meaning of Section 162(m) of the Internal Revenue Code.

2.4 Company means Eli Lilly and Company and its subsidiaries.

2.5 Company Bonus means the amount of bonus compensation payable to a Participant as described in Section 5 below. Notwithstanding the foregoing, however, the Committee may determine, in its sole discretion, to reduce the amount of a Participant's Company Bonus if such Participant becomes eligible to participate in such other bonus program of the Company as may be specifically designated by the Committee. Such reduction may be by a stated percentage up to and including 100% of the Company Bonus.

2.6 Company Performance Bonus Multiple means the amount as calculated in Sections 5.3 and 5.4 below.

2.7 Disabled means a Participant who (i) has become eligible for a payment under The Lilly Extended Disability Plan, assuming eligibility to participate in that plan, or (ii) for those employees ineligible to participate in The Lilly Extended Disability Plan, has become otherwise "disabled" under the applicable disability benefit plan or program for the Participant, or, in the event that there is no such disability benefit plan or program, has become disabled under applicable local law.

2.8 Earnings Per Share (EPS) means the diluted earnings per share of the Company as reported in the Company's "Consolidated Statements of Income" in accordance with generally accepted accounting principles and Section 3.4 below.

2.9 Earnings Per Share Growth (EPS Growth) means the percentage increase in EPS in the Applicable Year compared to the prior year.

2.10 Effective Date means January 1, 2004, as amended from time to time.

2.11 Eligible Employee means:

a. with respect to employees of Lilly or its Puerto Rican subsidiaries, a person (1) who is employed as an employee by the Company on a scheduled basis of twenty (20) or more hours per week and is scheduled to work at least five (5) months per year; and (2) who is receiving compensation, including temporary illness pay under Lilly's Illness Pay Program or similar short-term disability program, from the Company for services rendered as an employee. Notwithstanding anything herein to the contrary, the term "Eligible Employee" will not include:

(1) a person who has reached Retirement with the Company;

(2) a person who is Disabled;

(3) a person who is a “leased employee” within the meaning of Section 414(n) of the Internal Revenue Code of 1986, as amended, or whose basic compensation for services on behalf of the Company is not paid directly by the Company;

(4) a person who is classified as a “Fixed Duration Employee”, as that term is used by Lilly;

(5) a person who is classified as a special status employee because his employment status is temporary, seasonal, or otherwise inconsistent with regular employment status;

(6) a person who is eligible to participate in the Eli Lilly and Company Prem1er Rewards Plan or such other Company bonus or incentive program as may be specifically designated by the Committee or its designee; or

(7) a person who submits to the Committee in writing a request that he not be considered eligible for participation in the Plan or is a member of the Board of Directors of Lilly unless he or she is also an Eligible Employee.

(8) any other category of employees designated by the Committee in its discretion with respect to any Applicable Year.

b. with respect to those employees who are employed by the Company, but not by Lilly or a Puerto Rican subsidiary, an employee of the Company designated by the Committee as a Participant in the Plan with respect to any Applicable Year. In its discretion, the Committee may designate Participants either on an individual basis or by determining that all employees in specified job categories, classifications, levels, subsidiaries or other appropriate classification will be Participants.

c. Notwithstanding anything herein to the contrary, the term Eligible Employee will not include any person who is not so recorded on the payroll records of the Company, including any such person who is subsequently reclassified by a court of law or regulatory body as a common law employee of the Company. Consistent with the foregoing, and for purposes of clarification only, the term employee or Eligible Employee does not include any individual who performs services for the Company as an independent contractor or under any other non-employee classification.

2.12 Lilly means Eli Lilly and Company.

2.13 Lilly Executive Officer or Section 162(m) Participant means a Participant who has been designated by the Board of Directors of Lilly as an executive officer pursuant to Rule 3b-7 under the Securities Exchange Act of 1934, as amended. For purposes of this Plan, a Lilly Executive Officer will be considered a Section 162(m) Participant whether or not he is a "covered employee" under Section 162(m).

2.14 Participant means an Eligible Employee who is participating in the Plan.

2.15 Participant Earnings means (A) those amounts described below that are earned during the portion of the Applicable Year during which the employee is a Participant in the Plan:

(i) regular compensation (including applicable deferred compensation amounts), overtime, shift premiums and other forms of additional compensation determined by and paid currently pursuant to an established formula or procedure;

(ii) salary reduction contributions to The Lilly Employee Savings Plan or elective contributions under any similar tax-qualified plan that is intended to meet the requirements of Section 401(k) of the Internal Revenue Code or similar Company savings program;

(iii) elective contributions to any cafeteria plan that is intended to meet the requirements of Section 125 of the Internal Revenue Code or other pre-tax contributions to a similar Company benefit plan;

(iv) payments made under the terms of Lilly's Illness Pay Program or other similar Company or government-required leave program during an Applicable Year to a Participant who is on approved leave of absence and is receiving one hundred percent (100%) of his base pay; and

(v) other legally-mandated or otherwise required pre-tax deductions from a Participant's base salary.

(B) The term "Participant Earnings" does not include:

(i) compensation paid in lieu of earned vacation;

(ii) amounts contributed to the Retirement Plan or any other qualified plan, except as provided in clause (A)(ii), above;

(iii) payments made under the terms of Lilly's Illness Pay Program or other similar Company or government-required leave program during an Applicable Year to a Participant who is on approved leave of absence and is receiving less than the full amount of his base pay;

(iv) amounts paid under this Plan or other bonus or incentive program of the Company;

(v) payments made under The Lilly Severance Pay Plan or any other

severance-type benefit (whether company-sponsored or mandated by law) arising out of or relating to a Participant's termination of employment;

(vi) payments based upon the discretion of the Company;

(vii) in the case of a person employed by a Lilly subsidiary, foreign service, cost of living, or other allowances that would not be paid were the person employed by Lilly;

(viii) amounts paid as commissions, sales bonuses, or Market Premiums (as defined under the Retirement Plan); or

(ix) earnings with respect to the exercise of stock options or vesting of restricted stock.

2.16 Performance Benchmarks mean the amounts as calculated in Section 5.3 below. The Performance Benchmarks will be established after considering expected pharmaceutical peer group performance and based on performance measures as described in Section 5.2.

2.17 Plan means The Eli Lilly and Company Bonus Plan as set forth herein and as hereafter modified or amended from time to time. The Plan is an incentive compensation program and is not subject to the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), pursuant to Department of Labor Regulation Section 2510.3.

2.18 Plant Closing means the closing of a plant site or other Company location that directly results in termination of employment.

2.19 Reduction in Workforce means the elimination of a work group, functional or business unit or other broadly applicable reduction in job positions that directly results in termination of employment.

2.20 Retirement means the cessation of employment upon the attainment of age fifty-five with ten years of service (55 and 10) or at least eighty (80) points, as determined by the provisions of the Retirement Plan as amended from time to time, assuming eligibility to participate in that plan. For persons who are not participants in the Retirement Plan, Retirement means the cessation of employment as a retired employee under the applicable retirement benefit plan or program as provided by the Company or applicable law.

2.21 Retirement Plan means The Lilly Retirement Plan.

2.22 Sales means, for any Applicable Year, the consolidated net sales of the Company as set forth in the "Consolidated Statements of Income" as reported by the Company in accordance with generally accepted accounting principles and Section 3.4 below.

2.23 Sales Growth means the percentage increase in Sales in the Applicable Year compared to the prior year.

2.24 Section 162(m) means Section 162(m) of the Internal Revenue Code of 1986, as amended.

2.25 Service means the aggregate time of employment of an Eligible Employee by the Company.

SECTION 3. ADMINISTRATION

3.1 Committee. The Plan will be administered by the Compensation Committee of the Board of Directors of Eli Lilly and Company or, if the name of the Compensation Committee is changed, the Plan will be administered by such successor committee. For all Eligible Employees other than Lilly Executive Officers, the Compensation Committee may delegate all or a portion of its responsibilities within its sole discretion by resolution. Any reference in this Plan to the Committee or its authority will be deemed to include such designees (other than with respect to Lilly Executive Officers or a member of the Board of Directors or for purposes of Section 9).

3.2 Powers of the Committee. The Committee will have the right to interpret the terms and provisions of the Plan and to determine any and all questions arising under the Plan, including, without limitation, the right to remedy possible ambiguities, inconsistencies, or omissions by a general rule or particular decision. The Committee will have authority to adopt, amend and rescind rules consistent with the Plan, to make exceptions in particular cases to the rules of eligibility for participation in the Plan (except with respect to Lilly Executive Officers), and to delegate authority for approval of participation of any Eligible Employee except for Lilly Executive Officers or a member of the Board of Directors. The Committee will take all necessary action to establish annual Performance Benchmarks and approve the timing of payments, as necessary.

3.3 Certification of Results. Before any amount is paid under the Plan, the Committee will certify in writing the calculation of EPS, EPS Growth, Sales and Sales Growth (or other applicable performance measures) for the Applicable Year and the satisfaction of all other material terms of the calculation of the Company Performance Bonus Multiple and Company Bonus.

3.4 Adjustments for Significant Events. Not later than 90 days after the beginning of an Applicable Year, the Committee may specify with respect to Company Bonuses for the Applicable Year that the performance measures described in Section 5.2 will be determined before the effects of acquisitions, divestitures, restructurings or special charges or gains, changes in corporate capitalization, accounting changes, and/or events that are treated as extraordinary items for accounting purposes; provided that such adjustments shall be made only to the extent permitted by Section 162(m) in the case of Lilly Executive Officers.

3.5 Finality of Committee Determinations. Any determination by the Committee of Sales, Sales Growth, EPS, EPS Growth, any other performance measure, Performance Benchmarks and the level and entitlement to Company Bonus, and any interpretation, rule, or decision adopted by the Committee under the Plan or in carrying out or administering the Plan, will be final and binding for all purposes and upon all interested persons, their heirs, and personal representatives. The Committee may rely conclusively on determinations made by Lilly and its auditors to determine Sales, Sales Growth, EPS, EPS Growth and related information for administration of the Plan, whether such

information is determined by the Company, auditors or a third-party vendor engaged specifically to provide such information to the Company. This subsection is not intended to limit the Committee's power, to the extent it deems proper in its discretion, to take any action permitted under the Plan.

SECTION 4. PARTICIPATION IN THE PLAN

4.1 General Rule. Only Eligible Employees may participate in and receive payments under the Plan.

4.2 Commencement of Participation. An Eligible Employee will become a Participant in the Plan as follows: (i) in the case of Eligible Employees under Section 2.11(a), on the date on which the individual completes at least one hour of employment as an Eligible Employee within the United States or Puerto Rico, and (ii) in the case of Eligible Employees under Section 2.11(b), on the date as of which the Committee has designated the individual to become a Participant in the Plan.

4.3 Termination of Participation. An Eligible Employee will cease to be a Participant upon termination of employment with the Company for any reason, or at the time he otherwise ceases to be an Eligible Employee under the Plan.

SECTION 5. DEFINITION AND COMPUTATION OF COMPANY BONUS

5.1 Computation for Eligible Employees. Company Bonus amounts will depend significantly on Company performance as well as Participants' individual performance for certain Eligible Employees. As more specifically described below, a Participant's Company Bonus is calculated by multiplying the Participant's Bonus Target by his Participant Earnings and the Company Performance Bonus Multiple. For eligible management and Lilly employees and those Participants designated by the Committee, individual performance will also impact the Company Bonus calculation, as described in Section 5.6(c) below. Company Bonuses are paid out to eligible Participants in the manner provided below.

5.2 Establishment of Performance Measures. Not later than 90 days after the beginning of each Applicable Year, the Committee will, in its sole discretion, determine appropriate performance measures for use in calculating Company Bonus amounts. These performance measures may include Sales Growth, EPS Growth, growth in net income, return on assets, return on equity, total shareholder return, EVA, MVA or any of the foregoing before the effect of acquisitions, divestitures, accounting changes, restructurings and special charges or gains (determined according to objective criteria established by the Committee not later than ninety (90) days after the beginning of the Applicable Year). Unless otherwise specified in a written resolution adopted by the Committee for the Applicable Year, the Committee will use EPS Growth and Sales

Growth, in each case before the effect of acquisitions, divestitures, accounting changes, restructurings and special charges or gains (determined as described above) as performance measures.

5.3 Establishment of Performance Benchmarks. Not later than 90 days after the beginning of each Applicable Year, the Committee will establish Performance Benchmarks for the Company based on the performance measures described in Section 5.2 above. Unless otherwise specified in a written resolution adopted by the Committee for the Applicable Year, the Performance Benchmarks will correspond with EPS Growth and Sales Growth amounts for the Applicable Year, established after considering expected pharmaceutical peer group performance. The Performance Benchmarks will correspond to EPS Growth and Sales Growth multiples equal to 1.0. The Committee will also adopt a formula that will determine the extent to which the performance measure multiples will vary as the Company's actual results vary from the Performance Benchmarks.

5.4 Company Performance Bonus Multiple. Unless otherwise specified in a written resolution adopted by the Committee not later than 90 days after the beginning of the Applicable Year, the Company Performance Bonus Multiple is equal to the product of the EPS Growth multiple and 0.75 plus the product of the Sales Growth multiple and 0.25 (i.e., Company Performance Bonus Multiple = (EPS Growth multiple * 0.75) + (Sales Growth multiple * 0.25)).

5.5 Company Performance Bonus Multiple Threshold and Ceiling: Notwithstanding Sections 5.3 and 5.4, the Company Performance Bonus Multiple will not be less than 0.25 or greater than 2.0 in an Applicable Year. If the calculations described in Sections 5.3 and 5.4 above result in a number that is less than 0.25, the Company Performance Bonus Multiple will equal 0.25 for the Applicable Year. If the calculations described in Sections 5.3 and 5.4 above result in a multiple greater than 2.0, the Company Performance Bonus Multiple will equal 2.0 for the Applicable Year. Notwithstanding the foregoing, the Committee may reduce the Company Performance Bonus Multiple (including but not limited to a reduction to below 0.25) for some or all Eligible Employees, in its discretion.

5.6 Participant Company Bonus.

a. Bonus Target. Not later than 90 days after the beginning of the Applicable Year, the Bonus Target for each Participant will be determined by the Committee on a basis that takes into consideration a Participant's pay grade level and job responsibilities. The Bonus Target for each Participant for the Applicable Year will be expressed as a percentage of Participant Earnings as of December 31 of the Applicable Year. Early in the Applicable Year, each Participant will receive information regarding the Participant's Bonus Target. In the event that a Participant's pay grade level changes during the Applicable Year (e.g., because of promotion, demotion or otherwise), the Participant's Bonus Target will be prorated based on the Bonus Target applicable to

each pay grade level (with related job responsibilities) and the percentage of time that the Participant is employed at each pay grade level during the Applicable Year.

b. Company Bonus Calculation. Except as described in Section 5.6(c) below, a Participant's Company Bonus will equal the product of the Company Performance Bonus Multiple and the Participant's Bonus Target and the Participant's Earnings.

c. Adjustment for Performance Multiplier, if Applicable. Notwithstanding anything herein to the contrary, all eligible management employees (except Lilly Executive Officers), United States employees and other employees as may be designated from time to time by the Committee are subject to individual performance multipliers. For all such Participants subject to an individual performance multiplier, the amount calculated in Section 5.5(b) above will be adjusted based on the Participant's performance rating at the end of the Applicable Year as described below. For each such Participant, the performance rating will be determined by the Participant's supervision.

1. Exemplary Performance. If the Participant receives an exemplary or equivalent performance rating (using the applicable performance rating system then in effect for the Participant), the amount calculated in Section 5.6(b) will be multiplied by an amount determined by the Committee, not to exceed 1.5, to obtain the Participant's actual Company Bonus.

2. Satisfactory Performance. If the Participant receives a satisfactory or equivalent performance rating (using the applicable performance rating system then in effect for the Participant), the amount calculated in Section 5.6(b) will be multiplied by 1.0 so that the Participant's actual Company Bonus will equal the amount calculated in Section 5.6(b) above.

3. Unsatisfactory Performance. If the Participant receives a year-end unsatisfactory or equivalent performance rating (using the applicable performance rating system then in effect for the Participant), the amount calculated in Section 5.6(b) will be multiplied by 0.0 so that the Participant's actual Company Bonus will equal $0.00.

In the event that a Participant does not receive a year-end performance rating, but is eligible for a Company Bonus, the amount calculated in Section 5.6(b) will be multiplied by 1.0 so that the Participant's actual Company Bonus will be the amount calculated in Section 5.6(b) above.

5.7 Conditions on Company Bonus. Payment of any Company Bonus is neither guaranteed nor automatic. A Participant's Company Bonus is not considered to be any form of compensation, wages, or benefits, unless and until paid.

5.8 Required Employment. Except as provided below in this Section 5.8 or as otherwise designated by the Committee, if a Participant is not employed by the Company on the last day of the Applicable Year, or is otherwise not an Eligible Employee on that date, the Participant is not entitled to any Company Bonus payment under this Plan for that Applicable Year.

a. Leaves of Absence. A Participant who, on the last day of the Applicable Year, is on approved leave of absence under the Family and Medical Leave Act of 1993, military leave under the Uniformed Services Employment and Reemployment Rights Act, or such other approved leave of absence will be considered to be an Eligible Employee on that date for purposes of this Plan.

b. Transfer. An employee who is a Participant in this Plan for a portion of the Applicable Year and then transfers to a position within the Company in which he is ineligible to participate in this Plan, but who remains employed by the Company on the last day of the Applicable Year, will be treated as satisfying the last-day-of-Applicable Year requirement for purposes of this Plan. In that event, his Company Bonus will be based on his Participant Earnings for the portion of the Applicable Year in which the employee was a Participant in the Plan.

c. Retirement, Disability or Death. A Participant who was an Eligible Employee for some portion of the Applicable Year and then takes Retirement, becomes and remains Disabled through the end of the Applicable Year, or dies during the Applicable Year will be considered to satisfy the last-day-of-Applicable-Year requirement described in this Section 5.8 for purposes of this Plan.

d. Reallocation, Medical Reassignment, Plant Closing or Reduction in Workforce. A Participant who was an Eligible Employee for some portion of the Applicable Year and whose employment is terminated as a result of his failure to locate a position following his reallocation or medical reassignment in the United States, or a Plant Closing or Reduction in Workforce will be considered to satisfy the last-day-of-Applicable Year requirement described in this Section 5.8 for purposes of this Plan. The Committee or its designee’s determination regarding whether a Participant’s termination is a direct result of either a Plant Closing or a Reduction in Workforce will be final and binding.

e. Notice of Resignation. In addition, a Participant who submits a notice of resignation from employment with the Company prior to the end of the Applicable Year and whose effective date of resignation is two (2) weeks or less from the date of notice of resignation will be considered employed by the Company for purposes of this Plan until the end of his specified notice period.

5.9 New Participants. If an Eligible Employee began participation in the Plan during an Applicable Year and is eligible for a Company Bonus, his Company Bonus will be based on Participant Earnings earned after the employee became a Participant. An Eligible Employee who became assigned to a position eligible for a Company Bonus at any time other than the first of the month will become a Participant the first of the following month.

5.10 Section 162(m) Requirements, Bonus Maximum. In the case of Lilly Executive Officers, all determinations necessary for computing a Company Bonus for the Applicable Year, including establishment of all components of EPS, EPS Growth, Sales, Sales Growth, Company Performance Bonus Multiple and Bonus Target percentages, shall be made by the Committee not later than 90 days after the commencement of the Applicable Year. As and to the extent required by Section 162(m), the terms of a Company Bonus for a Lilly Executive Officer must state, in terms of an objective formula or standard, the method of computing the amount of compensation payable to the Lilly Executive Officer, and must preclude discretion to increase the amount of compensation payable that would otherwise be due under the terms of the award. Notwithstanding anything elsewhere in the Plan to the contrary, the maximum amount of the Company Bonus that may be payable to a Lilly Executive Officer in respect of any Applicable Year will be $7 million.

SECTION 6. TIME OF PAYMENT

6.1 General Rule. Payment under the Plan will be made prior to April 1 of the year following the Applicable Year.

6.2 Terminated Employee. Except as provided in Section 5.8 above, in the event an Eligible Employee's employment with the Company ends for any reason prior to the last day of the Applicable Year, he will not receive any Company Bonus for the Applicable Year.

6.3 Deceased Eligible Employee. In the event an Eligible Employee dies before payment under the Plan is made, the Committee may, in its sole discretion, authorize the Company to pay to his personal representative or beneficiary an amount not to exceed the amount established by the Committee to reflect the payment accrued at the date of death.

SECTION 7. ADMINISTRATIVE GUIDELINES

7.1 Establishment and Amendment by the Committee. The Committee may establish objective and nondiscriminatory written guidelines for administering those provisions of the Plan that expressly provide for the determination of eligibility, Company Bonus or benefits on the basis of rules established by the Committee. The Committee may, from time to time, amend or supplement the administrative guidelines established in accordance with this subsection 7.1. The administrative guidelines established or amended in accordance with this subsection 7.1 will not be effective to the extent that they materially increase the Plan's liability, or to the extent that they are inconsistent with, or purport to amend, any provision of the Plan set forth in a document other than such administrative guidelines.

7.2. Amendment by Board of Directors. Any administrative guidelines established by the Committee pursuant to subsection 7.1 may be amended or revoked by the Board of Directors, either prospectively or retroactively, in accordance with the general amendment procedures set forth in section 9 below.

SECTION 8. MISCELLANEOUS

8.1 No Vested Right. No employee, participant, beneficiary, or other individual will have a vested right to a Company Bonus or any part thereof until payment is made to him under Section 6.

8.2 No Employment Rights. No provision of the Plan or any action taken by the Company, the Board of Directors of the Company, or the Committee will give any person any right to be retained in the employ of the Company. The right and power of the Company to dismiss or discharge any Participant for any reason or no reason, with or without notice, is specifically reserved.

8.3 No Adjustments. After the certification of the calculation of EPS, EPS Growth, Sales, Sales Growth and any other material terms of the calculation of the Company Performance Bonus Multiple and Company Bonus for the Applicable Year as described in Section 3.3 above, no adjustments will be made to reflect any subsequent change in accounting, the effect of federal, state, or municipal taxes later assessed or determined, or otherwise. Notwithstanding the foregoing, the Company reserves the right to and, in appropriate cases, will, seek restitution of any Company Bonus awarded to a Lilly Executive Officer if:

a. The amount of the Company Bonus was calculated based upon the achievement of certain financial results that were subsequently the subject of a restatement of all or a portion of the Company's financial statements;

b. The Lilly Executive Officer engaged in intentional misconduct that caused or partially caused the need for such a restatement; and

c. The amount of the Company Bonus that would have been awarded to the Lilly Executive Officer had the financial results been properly reported would have been lower than the amount actually awarded.

This subsection is not intended to limit the Company's power to take such action as it deems necessary to remedy the misconduct, prevent its recurrence and, if appropriate, based on all relevant facts and circumstances, punish the wrongdoer in a manner it deems appropriate.

8.4 Other Representations. Nothing contained in this Plan, and no action taken pursuant to its provisions, will create or be construed to create a trust of any kind, or a fiduciary relationship between the Company and any employee, participant, beneficiary, legal representative, or any other person. Although Participants generally have no right to any payment from this Plan, to the extent that any Participant acquires a right to receive payments from the Company under the Plan, such right will be no greater than the right of an unsecured general creditor of the Company. All payments to be made hereunder will be paid from the general funds of the Company and no special or separate fund will

be established, and no segregation of assets will be made, to assure payment of such amount.

8.5 Tax Withholding. The Company will make such provisions and take such steps as it may deem necessary or appropriate for the withholding of all federal, state, local, and other taxes required by law to be withheld with respect to Company Bonus payments under the Plan, including, but not limited to, deducting the amount required to be withheld from the amount of cash otherwise payable under the Plan, or from salary or any other amount then or thereafter payable to an employee, Participant, beneficiary, or legal representative.

8.6 Currency. The Company Bonus will be based on the currency in which the highest portion of base pay is regularly paid. The Committee will determine the appropriate foreign exchange conversion methodology in its discretion.

8.7 Effect of Plan on other Company plans. Nothing contained in this Plan is intended to amend, modify, terminate, or rescind other benefit or compensation plans established or maintained by the Company. Whether and to what extent a Participant's Company Bonus is taken into account under any other plan will be determined solely in accordance with the terms of such plan.

8.8 Construction. This Plan and all the rights thereunder will be governed by, and construed in accordance with, the laws of the state of Indiana, without reference to the principles of conflicts of law thereof.

8.9 Notice. Any notice to be given to the Company or Committee pursuant to the provisions of the Plan will be in writing and directed to Secretary, Eli Lilly and Company, Lilly Corporate Center, Indianapolis, IN 46285.

SECTION 9. AMENDMENT, SUSPENSION, OR TERMINATION

The Board of Directors of the Company will have the right to amend, modify, suspend, revoke, or terminate the Plan, in whole or in part, at any time and without notice, by written resolution of the Board of Directors. The Committee also will have the right to amend the Plan, except that the Committee may not amend this Section 9. Solely to the extent deemed necessary or advisable by the Board (or the Committee) for purposes of complying with Section 162(m), the Board (or the Committee) may seek the approval by the Company's stockholders of the Plan or any amendments to the Plan or any aspect of the Plan or Plan amendments. Any such approval shall be obtained in a separate vote of stockholders, with approval by a majority of the votes cast on the issue, including abstentions to the extent abstentions are counted as voting under applicable state law and the Articles of Incorporation and By-laws of the Company. To the extent deemed necessary or advisable by the Board of Directors to comply with Section 162(m), the material terms of the performance measures used in calculating Company Bonus amounts will be disclosed to and reapproved by the stockholders of the Company no later than the Company's 2009 annual meeting.

EXHIBIT 10.2

ELI LILLY AND COMPANY

**2007 CHANGE IN CONTROL SEVERANCE PAY PLAN
FOR SELECT EMPLOYEES**

1. PURPOSE

This Eli Lilly and Company 2007 Change in Control Severance Pay Plan For Select Employees has been established by the Company to provide for the payment of severance pay and benefits to Eligible Employees whose employment with a Participating Employer terminates due to certain conditions created by a Change in Control of the Company. The purpose of the Plan is to assure a continuity in operations of the Company during a period of Change in Control by allowing employees to focus on their responsibilities to the Company knowing that they have certain financial security in the event of their termination of employment. The accomplishment of this purpose is in the best interests of the Company and its shareholders. The Plan replaces the Change in Control Severance Pay Plan for Select Employees that was originally adopted by the Board on March 1, 1995, and shall become operative immediately upon the expiration of such plan with respect to a Change in Control occurring on or after March 1, 2007.

2. DEFINITIONS

The terms defined in this Section 2 shall have the meanings given below:

(a) “Base Salary” means an Eligible Employee’s gross annualized rate of base salary at the time of any determination hereunder, before any deductions, exclusions or any deferrals or contributions under any Participating Employer plan or program, but excluding bonuses, incentive awards or compensation, employee benefits or any other non-salary form of compensation.

(b) “Board” means the Board of Directors of the Company.

(c) “Change in Control” has the meaning given in Section 3.

(d) “Code” means the Internal Revenue Code of 1986, as amended.

(e) “Committee” means the Compensation Committee of the Board, or such other committee appointed by the Board to perform the functions of the Committee under the Plan, provided that at all times the Committee shall be constituted solely of directors who are Continuing Directors (as defined in Section 3) to the extent any such directors remain on the Board and are willing to serve in such capacity.

(f) “Covered Termination” has the meaning given in Section 6.

(g) “Company” means Eli Lilly and Company, an Indiana corporation.

(h) “Eligible Employee” means a Tier I Employee or a Tier II Employee.

(i) “ERISA” means the Employee Retirement Income Security Act of 1974, as amended.

(j) “Exchange Act” means the Securities Exchange Act of 1934, as amended.

(k) “Participating Employer” has the meaning given in Section 4.

(l) “Plan” means this Eli Lilly and Company 2007 Change in Control Severance Pay Plan for Select Employees.

(m) “Retirement Age” means the date the Eligible Employee reaches age 65, unless the Company’s senior most officer responsible for the Human Resources department has approved a later date as the Retirement Age for the Eligible Employee.

(n) “Severance Period” means the two (2) year period immediately following a Covered Termination.

3. CHANGE IN CONTROL

For purposes of the Plan, a “Change in Control” of the Company shall be deemed to have occurred upon:

(a) the acquisition by any “person,” as that term is used in Sections 13(d) and 14(d) of the Exchange Act (other than (i) the Company, (ii) any subsidiary of the Company, (iii) any employee benefit plan or employee stock plan of the Company or a subsidiary of the Company or any trustee or fiduciary with respect to any such plan when acting in that capacity, or (iv) Lilly Endowment, Inc.) of “beneficial ownership,” as defined in Rule 13d-3 under the Exchange Act, directly or indirectly, of 15% or more of the shares of the Company’s capital stock the holders of which have general voting power under ordinary circumstances to elect at least a majority of the Board (or which would have such voting power but for the application of the Indiana Control Shares Statute) (“Voting Stock”); provided, however, that an acquisition of Voting Stock directly from the Company shall not constitute a Change in Control under this Section 3(a);

(b) the first day on which less than two-thirds of the total membership of the Board shall be Continuing Directors (as that term is defined in Article 13(f) of the Company’s Articles of Incorporation);

(c) consummation of a merger, share exchange, or consolidation of the Company (a “Transaction”), other than a Transaction which would result in the Voting Stock of the Company outstanding immediately prior thereto continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity) more than 60% of the Voting Stock of the Company or such surviving entity immediately after such Transaction;

(d) a complete liquidation of the Company or a sale or disposition of all or substantially all the assets of the Company, other than a sale or disposition of assets to any subsidiary of the Company;

(e) either (i) the Company shall have entered into a definitive agreement with any Person, which, if consummated, would result in a Change in Control as specified in paragraphs (a) through (d) of this Section 3 or (ii) any Person initiates a tender offer or exchange offer to acquire shares of the Voting Stock which, if consummated, would result in a Change in Control as specified in paragraphs (a) through (d) of this Section 3; provided, however, that if the Board shall make a final determination that such agreement, tender offer or exchange offer will not be consummated, the occurrence of any such event shall cease to constitute a Change in Control and the termination of employment of an Eligible Employee after such determination shall not be treated as a Covered Termination on the basis of such event; or

(f) the Board adopts a resolution to the effect that any Person has taken actions which, if consummated, would result in its having acquired effective control of the business and affairs of the Company; provided, however, that if the Board shall make a final determination that such actions will not be consummated, the occurrence of any such event shall cease to constitute a Change in Control and the termination of employment of an Eligible Employee after such determination shall not be treated as a Covered Termination on the basis of such event.

For purposes of this Section 3 only, the term "subsidiary" means a corporation or limited liability company of which the Company owns directly or indirectly fifty (50) percent or more of the voting power.

4. PARTICIPATING EMPLOYERS

A. Designation of Participating Employers. The Company and each subsidiary corporation of which the Company owns directly or indirectly one-hundred (100) percent of the voting power at the time of the Change in Control shall be Participating Employers under the Plan. In addition, the Committee may designate other affiliates of the Company as Participating Employers under the Plan, from time to time and under such terms and conditions, as shall be specified by an action in writing by the Committee. Such terms and conditions may impose limitations on the extent to which any such affiliate participates in the Plan (including but not limited to the duration of any such participation), but shall not provide rights or benefits to Eligible Employees that are broader than those set forth in the Plan. Any entity that is a Participating Employer at the time of a Change in Control shall continue to be a Participating Employer following a Change in Control, and any person, firm or business that is a successor to the business or interests of a Participating Employer following a Change in Control shall be treated as a Participating Employer under the Plan.

B. Limitations in Foreign Jurisdictions. Notwithstanding the foregoing or anything elsewhere in the Plan to the contrary, the Committee shall have the discretionary authority, as specified below, to exclude from participation or limit the participation of any Participating Employer with respect to individuals employed outside of the United States. The Committee shall exercise this authority only by an action in writing taken prior to a Change in Control on the basis of a good faith determination that, as a result of the specific effect of applicable local law or practice

with respect to the Plan or severance benefits generally, it would be in the best interests of the Company to so exclude or limit such participation. In addition, to the extent specified by an action in writing prior to a Change in Control, the Committee may offset the benefits provided under the Plan to any such Eligible Employee by benefits under severance arrangements that exist by reason of applicable local law or practice.

5. ELIGIBLE EMPLOYEES

All employees of the Participating Employers, including executive officers (as defined in Rule 3b-7 under the Exchange Act), who are classified by the Company as G-6 level (Executive Director) or above (or any successor classifications) immediately prior to the Change in Control shall be eligible to participate in the Plan and shall be considered an Eligible Employee for all purposes hereunder. Any person who is an Eligible Employee in accordance with the foregoing shall continue to be an Eligible Employee notwithstanding any change in his/her position or classification following a Change in Control, subject to Section 6 hereof relating to certain terminations of employment. The Committee shall notify each Eligible Employee of his/her participation in the Plan prior to the Change in Control.

6. COVERED TERMINATIONS

A. General. An Eligible Employee shall be treated as having suffered a "Covered Termination" hereunder if his/her employment is terminated, within a period of two (2) years immediately following the date of a Change in Control, by a Participating Employer other than for "Cause" or by the Eligible Employee for "Good Reason."

For purposes of the foregoing, the two (2) year time period specified above within which a termination of employment may be treated as a Covered Termination shall commence on the date the Change in Control becomes effective and, with respect to a Change in Control under paragraphs (e) and (f) of Section 3, shall recommence (for the full applicable period) on the date of consummation of the underlying actions. For purposes of the Plan, a termination of employment shall be effective as of the last date of the Eligible Employee's employment with the Participating Employer.

An Eligible Employee shall not be treated as having suffered a Covered Termination in the event of (1) death, (2) total disability (within the meaning of the Company's Extended Disability Plan), (3) transfer of employment among Participating Employers (unless such transfer gives rise to a "Good Reason"), (4) involuntary termination by the Participating Employer for "Cause", (5) voluntary termination by the Eligible Employee other than for Good Reason, (6) a termination of employment for any reason by either the Participating Employer or the Eligible Employee that does not occur during the time periods specified above or (7) a termination of employment for any reason by either the Participating Employer or the Eligible Employee after the Eligible Employee reaches Retirement Age.

B. Termination For Cause. For purposes hereof, the termination of an Eligible Employee's employment shall be deemed to be a termination for "Cause" if as a result of:

(i) the willful refusal of the Eligible Employee to perform, without legal cause, his/her material duties to the Participating Employer, resulting in demonstrable economic harm to any Participating Employer, which the Eligible Employee has failed to cure after thirty (30) calendar days' advance written notice from the Company;

(ii) any act of fraud, dishonesty or gross misconduct of the Eligible Employee resulting in significant economic harm to any Participating Employer or other significant harm to the business reputation of any Participating Employer; or

(iii) the conviction of the Eligible Employee by a court of competent jurisdiction of any crime (or the entering of a plea of guilty or nolo contendere to a charge of any crime) constituting a felony.

A termination for Cause shall be communicated to the Eligible Employee in writing by the Participating Employer and shall specify the provisions of the Plan and factual matters relied upon in making the Cause determination.

C. Termination for Good Reason. For purposes hereof, an Eligible Employee may terminate his/her employment for "Good Reason" as a result of:

(i) a material diminution in the nature or status of the Eligible Employee's position, title, reporting relationship, duties, responsibilities or authority, or the assignment to him/her of additional responsibilities that materially increase his/her workload;

(ii) any reduction in the Eligible Employee's then-current Base Salary;

(iii) a material reduction in the Eligible Employee's opportunities to earn incentive bonuses below those in effect for the year most recently completed before the date of the Change in Control, taking into account all material bonus factors such as targeted bonus amounts and corporate performance measures;

(iv) a material reduction in the Eligible Employee's employee benefits and coverages (including, without limitation, pension, profit sharing and all welfare, retiree welfare and fringe benefits) that are provided to the Eligible Employee from the benefit levels in effect immediately prior to the Change in Control;

(v) the failure to grant to the Eligible Employee stock options, stock units, performance shares or similar incentive rights during each twelve (12) month period following the Change in Control on the basis of a number of shares or units and all other material terms (including vesting requirements) at least as favorable to the Eligible Employee as those rights granted to him/her on an annualized average basis for the three (3) year period immediately prior to the Change in Control;

(vi) relocation of the Eligible Employee by more than fifty (50) miles from his/her regularly assigned workplace existing immediately prior to the date of the Change in Control; or

(vii) any failure by a successor entity to the Company (including any entity that succeeds to the business or assets of the Company) in connection with a Change in Control to assume by operation of law or otherwise the obligations of the Company under the Plan, or any attempted amendment, termination or repudiation of the Plan by such successor entity, other that pursuant to the provisions of Section 15.

For purposes of the foregoing, but without limitation of the Eligible Employee's right to otherwise terminate employment for Good Reason, if the Eligible Employee is in charge of a principal business unit, division or function of the Company immediately prior to a Change in Control, Good Reason shall not be deemed to exist based solely on the fact that the Eligible Employee is not in charge of such principal business unit, division or function of the combined entity following the Change in Control, unless as a result thereof, the Eligible Employee suffers a material diminution in the nature or status of the Eligible Employee's position, title, reporting relationship, duties, responsibilities or authority or suffers some other Good Reason event.

A termination for Good Reason shall be communicated to the Participating Employer in writing by the Eligible Employee within thirty (30) days following his/her knowledge of the circumstances constituting Good Reason, and shall specify the provisions of the Plan and the factual matters relied upon in making the Good Reason determination. The Participating Employer shall have the opportunity to cure the circumstances constituting Good Reason within 15 days following receipt of such written notice from the Eligible Employee, and if such circumstances are fully cured, such circumstances shall cease to constitute the basis for a Good Reason termination hereunder.

7. SEVERANCE PAYMENT

The amount of the severance payment to be received by an Eligible Employee whose employment is terminated under conditions constituting a Covered Termination shall equal two (2) times the sum of:

(i) the Eligible Employee's Base Salary at the time of Covered Termination (calculated without regard to any reduction in Base Salary that results in a Good Reason termination) or, if greater, at the time of the Change in Control, *plus*

(ii) the greater of (a) the amount of the Eligible Employee's target annual cash incentive bonus for the year of Covered Termination or (b) the amount of the Eligible Employee's annual cash incentive bonus earned for the year immediately prior to the Change in Control.

The severance payment to be made hereunder shall be paid to the Eligible Employee in a single lump-sum cash payment, less any required tax withholding, within thirty (30) calendar days after the date of the Eligible Employee's Covered Termination. Any payment required under this Section 7 or any other provision of the Plan that is not made in a timely manner shall bear interest at a rate equal to one hundred twenty (120) percent of the monthly compounded applicable federal rate, as in effect under Section 1274(d) of the Code for the month in which the payment is required to be made.

8. OTHER SEVERANCE BENEFITS

In addition to the severance payment provided under Section 7, an Eligible Employee shall be entitled to the following benefits and other rights in the event of his/her Covered Termination:

A. Welfare Benefits. The Eligible Employee shall be entitled to continued coverage and benefits for the duration of the Severance Period under the Participating Employer's medical and dental plans, group life insurance plans, company-provided death benefit, supplemental life insurance and long-term disability plans for which he/she was eligible at the time of Covered Termination (or, if it would provide benefits or other terms more favorable to the Eligible Employee, at the time of the Change in Control), as though his/her termination of employment had not occurred (the "Welfare Continuation Coverages"). All Welfare Continuation Coverages shall apply to the Eligible Employee and any of his/her dependents who would have been eligible for coverage if the Eligible Employee remained employed for the Severance Period. The Company may provide the Eligible Employee with the Welfare Continuation Coverages under arrangements other than its generally applicable welfare benefit plans, provided that the benefit coverages so provided are at least as favorable to the Eligible Employee as coverage under the otherwise applicable Welfare Continuation Coverages, on a coverage by coverage basis, and taking into account all tax consequences to the Eligible Employee. At the expiration of the Severance Period, the Eligible Employee shall be treated as a then terminating employee with respect to the right to elect continued medical and dental coverages in accordance with Section 4980B of the Code (or any successor provision thereto).

B. Retiree Welfare Benefits. For purposes of determining eligibility for the retiree medical and dental plans applicable to Eligible Employee (the "Retiree Welfare Plans"), the Eligible Employee shall receive additional credit for the number of years equal to the Severance Period for purposes of both age and service requirements under the Retiree Welfare Plans, but not beyond the Retirement Age of the Eligible Employee. If an Eligible Employee shall be eligible for participation in the Retiree Welfare Plans at the time of Covered Termination (including by reason of this Section 8.B.), then (i) for the Severance Period, he/she shall be entitled to continue to participate in either the Retiree Welfare Plans or the Welfare Continuation Coverage pursuant to Section 8.A. hereof, whichever provides greater benefits to the Eligible Employee on a coverage by coverage basis, and (ii) following the Severance Period, he/she shall be entitled to continue to participate in the retiree welfare benefit program provided to retired employees of the Participating Employer generally, or if no such program is provided, the program of the successor entity following the Change in Control, if any.

C. Pension Supplement. The Eligible Employee shall be entitled to the additional pension benefits that would be payable to him/her, under all defined benefit pension plans of a Participating Employer in which he/she is participating at the time of Covered Termination (or, if it would provide benefits or other terms more favorable to the Eligible Employee, at the time of the Change in Control), including all such tax-qualified and supplemental plans, by taking into account under such plans (i) an additional number of years equal to the Severance Period for purposes of the age and service credit of the Eligible Employee under such plans and (ii) the amount of the severance payment to which the Eligible Employee is entitled under Section 7, expressed on an annualized basis for the number of years equal to the Severance Period, for purposes of the compensation credit

of the Eligible Employee under such plans (but only to the extent such additional credit would produce a higher benefit for the Eligible Employee than if it were not taken into account). The additional pension benefits provided hereby shall be paid pursuant to a supplemental pension plan of the Company, at the same time and in the same form as pension benefits are otherwise payable to the Eligible Employee (subject to clause (iii) of Section 8.E). Notwithstanding the foregoing, the Eligible Employee will only receive additional age, service and compensation credit hereunder until his/her Retirement Age.

D. Equity Incentives. Immediately upon a Covered Termination, (i) any stock options, or similar equity-based incentive rights granted to the Eligible Employee under a stock incentive plan of a Participating Employer that are not then fully vested and exercisable shall become fully vested and immediately exercisable, (ii) the Eligible Employee shall be entitled to exercise any stock options or similar equity-based incentive rights until the expiration of three years following the date of the Covered Termination (or until such later date as may be applicable under the terms of the option or other right upon termination of employment), subject to the maximum full term of the option but without regard to any earlier termination otherwise applicable in the event of termination of employment, and (iii) any performance shares, stock units or shares of restricted stock granted to the Eligible Employee under a stock incentive plan of a Participating Employer that remain subject to forfeiture, performance conditions or transfer restrictions at such time shall become fully and immediately vested and all such conditions and restrictions shall immediately lapse. In addition, as to any other types of equity-based incentive awards granted to the Eligible Employee under a stock incentive plan of a Participating Employer prior to the date of Covered Termination, any restrictions on exercise, payment or transfer shall immediately lapse, and the Eligible Employee shall have all rights associated with such awards as of the date of Covered Termination. The provisions of this Section 8.D shall apply equally to any awards or rights into which the equity incentive rights described herein are converted or for which such rights are substituted in connection with a Change in Control.

E. Accrued Rights. The Eligible Employee shall be entitled to the following payments and benefits in respect of accrued compensation rights at the time of a Covered Termination, in addition to all other rights provided under the Plan: (i) immediate payment of any accrued but unpaid Base Salary through the date of Covered Termination; (ii) payment within fifteen (15) calendar days of Covered Termination of the accrued annual cash bonus for the year in effect on the date of the Covered Termination, determined on the basis of the bonus earned under terms of the applicable bonus plan through the date of termination or, if greater, the pro-rata amount of the target annual cash bonus for the period of such year through the date of termination; (iii) payment within fifteen (15) calendar days of Covered Termination of all non-tax-qualified deferred compensation rights, in lieu of payment in respect of such rights that would otherwise be made at a later date in accordance with the terms of such arrangements, except to the extent such rights are funded by amounts held under an irrevocable grantor trust or other irrevocable commitment of funds by the Company; and (iv) all benefits and rights accrued under the employee benefit plans, fringe benefit programs and payroll practices of a Participating Employer (other than those described in clause (iii) above) in accordance with their terms (including, without limitation, employee pension, employee welfare, incentive bonus and stock incentive plans).

F. Outplacement; Relocation. The Eligible Employee shall be provided, at the Company's sole expense, with professional outplacement services selected by the Eligible Employee consistent with his/her duties or profession and of a type and level customary for persons in his/her position; provided, however, that the Company shall not be required to pay fees in connection with the foregoing in an amount greater than fifteen (15) percent of the Eligible Employee's Base Salary for purposes of clause (i) of Section 7. The Company shall honor any prior agreement or understanding with an Eligible Employee who has suffered a Covered Termination to reimburse his/her relocation expenses to the Indianapolis, Indiana metropolitan area or, if it does not result in a greater cost to the Company, to such other location selected by the Eligible Employee.

G. Indemnification. With respect to any Eligible Employee who is, immediately prior to a Change in Control or a Covered Termination, indemnified by the Company for his/her service as a director, officer or employee of a Participating Employer, the Company shall indemnify such Eligible Employee to the fullest extent permitted by applicable law, and the Company shall maintain in full force and effect, for the duration of all applicable statute of limitation periods, insurance policies at least as favorable to the Eligible Employee as those maintained by the Company for the benefit of its directors and officers at the time of Change in Control, provided that such insurance policies are commercially available from carriers of recognized standing, with respect to all costs, charges and expenses whatsoever (including payment of expenses in advance of final disposition of a proceeding) incurred or sustained by the Eligible Employee in connection with any action, suit or proceeding to which he/she may be made a party by reason of being or having been a director, officer or employee of a Participating Employer or serving or having served any other enterprise as a director, officer or employee at the request of a Participating Employer.

H. Retention Bonuses and Loans. Immediately upon a Covered Termination, there shall automatically be forgiven any repayment obligation of the Eligible Employee to the Participating Employer that arises under any retention bonus agreement, forgivable loan or similar arrangement that provides for the lapse of the Eligible Employee's repayment obligation over time based on continued employment or other conditions (but not under any other loan obligations of the Eligible Employee that do not include forgiveness provisions).

9. EXCISE TAX REIMBURSEMENT

(a) In the event it shall be determined that any payment, right or distribution by the Company or any other person or entity to or for the benefit of an Eligible Employee pursuant to the terms of this Plan or otherwise, in connection with, or arising out of, his/her employment with a Participating Employer or a change in ownership or effective control of the Company or a substantial portion of its assets (a "Payment") is a "parachute payment" within the meaning of Section 280G of the Code on account of the aggregate value of the Payments due to the Eligible Employee being equal to or greater than three times the "base amount," as defined in Section 280G(b)(3) of the Code, (the "Parachute Threshold") so that the Eligible Employee would be subject to the excise tax imposed by Section 4999 of the Code (the "Excise Tax"), concurrent with the making of such Payment, then (i) in the event the aggregate value of the Payments exceeds the Parachute Threshold by less than 3%, one or more Payments shall be reduced so that the aggregate value of the Payments is $1.00 less than the Threshold Amount, or (ii) in the event that the aggregate value of the Payments exceeds the Parachute Threshold by 3% or more, the Company

shall pay to the Eligible Employee an additional payment (the "Gross-Up Payment") in an amount such that the net amount retained by the Eligible Employee, after deduction of any Excise Tax on such Payments and any federal, state or local income tax and Excise Tax on the Gross-Up Payment shall equal the amount of such Payments. In the event the Internal Revenue Service subsequently may assess or seek to assess from the Eligible Employee an amount of Excise Tax in excess of that determined in accordance with the foregoing, the Company shall pay to the Eligible Employee an additional Gross-Up Payment, calculated as described above in respect of such excess Excise Tax, including a Gross-Up Payment in respect of any interest or penalties imposed by the Internal Revenue Service with respect to such excess Excise Tax. The rights of the Eligible Employee to a Gross-Up Payment under this Section 9 shall apply without regard to whether the Eligible Employee has incurred a Covered Termination and shall apply to all payments whether or not in connection with a Covered Termination.

(b) All determinations required to be made under this Section 9, including whether any Payment is a "parachute payment" and whether and when a Gross-Up Payment is required and the amount of such Gross-Up Payment and the assumptions to be utilized in arriving at such determination, shall be made by a nationally recognized accounting firm designated by the Company which is not the auditor of the Company or another party involved in the Change in Control (the "Accounting Firm") and shall be based upon "substantial authority" (within the meaning of Section 6662 of the Code). The Accounting Firm shall provide detailed supporting calculations both to the Company and the Eligible Employee within 15 business days of the receipt of notice from the Company or an Eligible Employee that there has been a Payment, or such earlier time as is requested by the Company. All fees and expenses of the Accounting Firm shall be borne by the Company. Any Gross-Up Payment, as determined pursuant to this Section 9, shall be paid by the Company to the Eligible Employee within five business days of the receipt of the Accounting Firm's determination. Any determination by the Accounting Firm shall be binding upon the Company and the Eligible Employee.

10. RELEASE OF CLAIMS

All payments and benefits that may be made to an Eligible Employee upon a Covered Termination under the Plan shall be contingent upon the Eligible Employee entering into a general release of employment law claims against the Company in substantially the form attached hereto as Exhibit A, subject to such modifications as may be determined by the Committee in good faith to take into account changes in employment laws or differences in employment laws in other jurisdictions.

11. NO MITIGATION OR OFFSET

The Eligible Employee shall be under no obligation to minimize or mitigate damages by seeking other employment, and the obtaining of any such other employment shall in no event effect any reduction of the Company's obligation to make the payments and provide the benefits required under the Plan. Except as provided in Section 10, the Company's obligation to make the payments and provide the benefits required under the Plan shall not be affected by any circumstances, including, without limitation, any set-off, counterclaim, recoupment, defense or other rights which a Participating Employer may have against the Eligible Employee.

12. UNFUNDED STATUS

The Plan is intended to constitute an employee pension benefit plan under ERISA which is unfunded and is maintained primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees, and shall be interpreted and administered accordingly. The payments and benefits provided hereunder shall be paid from the general assets of the Company. Nothing herein shall be construed to require the Company to maintain any fund or to segregate any amount for the benefit of any employee, and no employee or other person shall have any right against, right to, or security or other interest in any fund, account or asset of the Company from which the payment pursuant to the Plan may be made. Consistent with the foregoing, the Company may, in its sole discretion, deposit funds in a grantor trust or otherwise establish arrangements to pay amounts that become due under the Plan, and, notwithstanding anything elsewhere in the Plan to the contrary, the payments and benefits due under the Plan shall be reduced to reflect the amount of any payment made in respect of any Eligible Employee from a grantor trust or other arrangement established for this purpose.

13. ADMINISTRATION

The Committee shall be the named fiduciary of the Plan and the plan administrator for purposes of ERISA. The Committee shall be responsible for the overall operation of the Plan and shall have the fiduciary responsibility for the general operation of the Plan. The Committee may allocate to any one or more of the Company's employees any responsibility the Committee may have under the Plan and may designate any other person or persons to carry out any of the Committee's responsibilities under the Plan. As plan administrator, the Committee shall maintain records pursuant to the Plan's provisions and shall be responsible for the handling, processing and payment of any claims for benefits under the Plan.

14. CLAIMS AND DISPUTES

Within fifteen (15) calendar days following a Covered Termination, the Company shall notify each Eligible Employee whom the Company determines is entitled to payments and benefits under the Plan of his/her entitlement to such payments and benefits. An Eligible Employee who is not so notified may submit a claim for payments and benefits under the Plan in writing to the Company within ninety (90) calendar days after becoming entitled to such benefits as described in Section 6. All such claims shall be approved or denied in writing by the Company within fifteen (15) calendar days after submission.

Any denial of a claim by the Company shall be in writing and shall include: (i) the reason or reasons for the denial; (ii) reference to the pertinent Plan provisions on which the denial is based; (iii) a description of any additional material or information necessary for the Eligible Employee to perfect the claim together with an explanation of why the material or information is necessary; and (iv) an explanation of the Plan's claim review procedure, described below.

An Eligible Employee shall have a reasonable opportunity to appeal a denied claim to the Company for a full and fair review. The Eligible Employee or authorized representative shall have sixty (60) calendar days after receipt of written notification of the denial of claim in which to request a review and to review pertinent documents of the Plan. The Company shall notify the Eligible Employee or his/her authorized representative of the time and place for the claim review. The Company shall issue a decision on the reviewed claim promptly, but no later than fifteen (15) calendar days after receipt of the request for review. The Company's decision shall be in writing and shall include: (i) the reasons for the decision, and (ii) references to the Plan provisions on which the decision is based.

If the Eligible Employee shall dispute the Company's final decision, the dispute shall be submitted to an arbitration proceeding, conducted before a panel of three arbitrators, in accordance with the rules of the Center for Public Resources (or such other organization selected by mutual agreement of the Company and the Eligible Employee). Such arbitration shall take place in the location most practicably proximate to the Eligible Employee's principal workplace. Judgment may be entered on the arbitrators' award in any court having jurisdiction. Notwithstanding the foregoing, if an Eligible Employee believes the claims procedure or dispute resolution mechanism provided under this Section 14 would be futile or would cause such Eligible Employee irreparable harm, the Eligible Employee may, in his/her sole discretion, elect to enforce his/her rights under the Plan pursuant to Section 502 of ERISA.

The Company shall bear the expense of any enforcement proceeding brought by an Eligible Employee under the Plan and shall reimburse the Eligible Employee for all of his/her reasonable costs and expenses relating to such enforcement proceeding, including, without limitation, reasonable attorneys' fees and expenses, provided that the Eligible Employee is the prevailing party in such proceeding. For purposes hereof, the trier of fact in such enforcement proceeding shall be requested to make a determination as to the reimbursement of the Eligible Employee's costs and expenses as a prevailing party hereunder. In no event shall the Eligible Employee be required to reimburse the Company for any of the costs or expenses relating to such enforcement proceeding.

15. TERM AND AMENDMENT

The Plan shall become effective as on July 1, 2004, but shall only be operative with respect to a Change in Control occurring on or after March 1, 2007, the date as of which the Plan as previously in effect shall have been terminated by action of the Board. The Plan shall continue to be effective until terminated in accordance with this Section 15. The Board shall have the right, by resolution or other written action, to terminate or amend the Plan; provided, however, that the Plan

may only be terminated or amended prior to a Change in Control, and then only (i) with respect to an amendment or termination that becomes effective upon the second (2nd) anniversary of notice being given thereof to Eligible Employees generally, or (ii) to the extent any such amendment is of a technical or clarifying nature, or increases the rights or benefits of all affected Eligible Employees, and does not in any manner reduce the rights or benefits of any Eligible Employee, unless the Company has obtained the express written consent, in return for good and valuable consideration, of all affected Eligible Employees in respect of any such amendment. Notwithstanding the foregoing, in the event of a Change in Control, the Plan shall continue in effect, and no termination or amendment of the Plan shall occur, until the satisfaction of all severance payments and benefits to which Eligible Employees are or may become entitled to under the Plan. Upon the occurrence of a Change in Control during the term of the Plan, the Plan shall not be operative with respect to any subsequent Change in Control.

16. SUCCESSORS AND ASSIGNS

The Plan shall be binding upon any person, firm or business that is a successor to the business or interests of the Company, whether as a result of a Change in Control of the Company or otherwise. Any successor to the Company shall be required to assume the Plan in writing and honor the obligations of the Company and the Participating Employers hereunder. All payments and benefits that become due to an Eligible Employee under the Plan shall inure to the benefit of his/her heirs, assigns, designees or legal representatives.

17. ENFORCEABILITY

The Company intends the Plan to constitute a legally enforceable obligation between it and each Eligible Employee, and that the Plan confer vested rights on each Eligible Employee in accordance with the terms of the Plan, with each Eligible Employee being a third-party beneficiary thereof. Nothing in the Plan, however, shall be construed to confer on any Eligible Employee any right to continue in the employ of a Participating Employer or affect the right of a Participating Employer to terminate the employment or change the terms and conditions of employment of an Eligible Employee, with or without notice or cause, prior to a Change in Control, or to take any such action following a Change in Control, subject to the consequences specified by the Plan.

The Plan shall be construed and enforced in accordance with ERISA and the laws of the State of Indiana to the extent not preempted by ERISA, regardless of the law that might otherwise govern under applicable principles or provisions of choice or conflict of law doctrines. To the extent any provision of the Plan shall be invalid or unenforceable under any applicable law, it shall be considered deleted herefrom and all other provisions of the Plan shall be unaffected and shall continue in full force and effect.

EXHIBIT 11. STATEMENT RE: COMPUTATION OF EARNINGS PER SHARE

(Unaudited)

ELI LILLY AND COMPANY AND SUBSIDIARIES

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
	(Dollars and shares in millions except per-share data)			
BASIC				
Net income	$ 873.6	$ 794.4	$ 2,530.4	$ 1,279.0
Average number of common shares outstanding	1,085.2	1,088.6	1,085.0	1,087.6
Contingently issuable shares	.4	.3	.4	.2
Adjusted average shares	1,085.6	1,088.9	1,085.4	1,087.8
Basic earnings per share	$ .80	$ .73	$ 2.33	$ 1.18
DILUTED				
Net income	$ 873.6	$ 794.4	$ 2,530.4	$ 1,279.0
Average number of common shares outstanding	1,085.2	1,088.6	1,085.0	1,087.6
Incremental shares — stock options and contingently issuable shares	1.2	2.8	1.4	3.5
Adjusted average shares	1,086.4	1,091.4	1,086.4	1,091.1
Diluted earnings per share	$ .80	$ .73	$ 2.33	$ 1.17

EXHIBIT 12. STATEMENT RE: COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES
(Unaudited)

ELI LILLY AND COMPANY AND SUBSIDIARIES
(Dollars in millions)

	Nine Months Ended September 30, 2006	Years Ended December 31, 2005	2004	2003	2002	2001
Consolidated pretax income before cumulative effect of a change in accounting principle	$ 3,203.0	$ 2,717.5	$ 2,941.9	$ 3,261.7	$ 3,457.7	$ 3,506.9
Interest	273.1	245.7	162.9	121.9	140.0	253.3
Less interest capitalized during the period	(79.6)	(140.5)	(111.3)	(60.9)	(60.3)	(61.5)
Earnings	$ 3,396.5	$ 2,822.7	$ 2,993.5	$ 3,322.7	$ 3,537.4	$ 3,698.7
Fixed charges	$ 273.1	$ 245.7	$ 162.9	$ 121.9	$ 140.0	$ 253.3
Ratio of earnings to fixed charges	12.4	11.5	18.4	27.3	25.3	14.6

EXHIBIT 31.1 Rule 13a-14(a) Certification of Sidney Taurel, Chairman of the Board and Chief Executive Officer

CERTIFICATIONS

I, Sidney Taurel, chairman of the board and chief executive officer, certify that:

1. I have reviewed this report on Form 10-Q of Eli Lilly and Company;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's Board of Directors (or persons performing the equivalent function):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: November 1, 2006

By: /s/Sidney Taurel
Sidney Taurel
Chairman of the Board
and Chief Executive Officer

EXHIBIT 31.2 Rule 13a-14(a) Certification of Derica W. Rice, Senior Vice President and Chief Financial Officer

CERTIFICATIONS

I, Derica W. Rice, senior vice president and chief financial officer, certify that:

1. I have reviewed this report on Form 10-Q of Eli Lilly and Company;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's Board of Directors (or persons performing the equivalent function):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: November 1, 2006

By: /s/Derica W. Rice
Derica W. Rice
Senior Vice President
and Chief Financial Officer

EXHIBIT 32. Section 1350 Certification

Pursuant to section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code), each of the undersigned officers of Eli Lilly and Company, an Indiana corporation (the "Company"), does hereby certify that, to the best of their knowledge:

The Quarterly Report on Form 10-Q for the quarter ended September 30, 2006 (the "Form 10-Q") of the Company fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 and information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date November 1, 2006

/s/Sidney Taurel
Sidney Taurel
Chairman of the Board and Chief Executive Officer

Date November 1, 2006

/s/Derica W. Rice
Derica W. Rice
Senior Vice President and Chief Financial Officer