

LILLY ELI & CO
Form DEF 14A
March 13, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of the Securities
Exchange Act of 1934 (Amendment No.)

Filed by the Registrant ☒
Filed by a Party other than the Registrant ☐

Check the appropriate box:

- ☐ Preliminary Proxy Statement
- ☐ **Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
- ☒ Definitive Proxy Statement
- ☐ Definitive Additional Materials
- ☐ Soliciting Material Pursuant to §240.14a-12

ELI LILLY AND COMPANY

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

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Notice of 2006 Annual Meeting and Proxy Statement

March 13, 2006

Dear Shareholder:

You are cordially invited to attend our annual meeting of shareholders on Monday, April 24, 2006, at the Lilly Center Auditorium, Lilly Corporate Center, Indianapolis, Indiana, at 11:00 a.m. EDT. If you are unable to attend in person, please join us via live webcast on the company's website at www.lilly.com. The webcast will be available for replay for 30 days.

The notice of meeting and proxy statement that follow describe the business we will consider at the meeting. Your vote is very important. I urge you to vote by mail, by telephone, or on the Internet in order to be certain your shares are represented at the meeting, even if you plan to attend.

Please note our procedures for admission to the meeting described on page 5.

I look forward to seeing you at the meeting.

Sidney Taurel

Chairman of the Board and Chief Executive Officer

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Notice of Annual Meeting of Shareholders

April 24, 2006

The annual meeting of shareholders of Eli Lilly and Company will be held at the Lilly Center Auditorium, Lilly Corporate Center, Indianapolis, Indiana, on Monday, April 24, 2006, at 11:00 a.m. EDT for the following purposes:

- to elect four directors of the company to serve three-year terms

- to ratify the appointment by the audit committee of Ernst & Young LLP as principal independent auditors for the year 2006

- to consider and vote on a shareholder proposal requesting that the board of directors report on the feasibility of extending our Animal Care and Use Policy to contract laboratories

- to consider and vote on a shareholder proposal requesting that the board of directors establish a policy of separating the roles of chairman and chief executive officer

- to consider and vote on a shareholder proposal requesting that the board of directors implement annual election of each director

- to consider and vote on a shareholder proposal requesting that the board of directors amend the company's articles of incorporation to elect directors by a majority of votes cast.

Shareholders of record at the close of business on February 15, 2006, will be entitled to vote at the meeting and at any adjournment of the meeting.

Attendance at the meeting will be limited to shareholders, those holding proxies from shareholders, and invited guests from the media and financial community. A page at the back of this proxy statement contains an admission ticket. If you plan to attend the meeting, please bring this ticket with you.

This combined proxy statement and annual report to shareholders and the proxy are being mailed on or about March 13, 2006.

By order of the board of directors,

James B. Lootens

Secretary

March 13, 2006

Indianapolis, Indiana

General Information

Why did I receive this proxy statement?

The board of directors of Eli Lilly and Company is soliciting proxies to be voted at the annual meeting of shareholders (the annual meeting) to be held on Monday, April 24, 2006, and at any adjournment of the annual meeting. When the company asks for your proxy, we must provide you with a proxy statement that contains certain information specified by law.

What will the shareholders vote on at the annual meeting?

Six items:

- election of directors

- ratification of the appointment of principal independent auditors

- a shareholder proposal on extending the company's Animal Care and Use Policy to contract laboratories

- a shareholder proposal on separating the roles of chairman and chief executive officer

- a shareholder proposal on annual election of each director

- a shareholder proposal on election of directors by majority vote.

Will there be any other items of business on the agenda?

We do not expect any other items of business because the deadline for shareholder proposals and nominations has already passed. Nonetheless, in case there is an unforeseen need, the accompanying proxy gives discretionary authority to the persons named on the proxy with respect to any other matters that might be brought before the meeting. Those persons intend to vote that proxy in accordance with their best judgment.

Who is entitled to vote?

Shareholders as of the close of business on February 15, 2006 (the record date), may vote at the annual meeting. You have one vote for each share of common stock you held on the record date, including shares:

- held directly in your name as the shareholder of record

- held for you in an account with a broker, bank, or other nominee

- attributed to your account in the Lilly Employee 401(k) Plan (the 401(k) plan).

What constitutes a quorum?

A majority of the outstanding shares, present or represented by proxy, constitutes a quorum for the annual meeting. As of the record date, 1,129,982,580 shares of company common stock were issued and outstanding.

How many votes are required for the approval of each item?

There are differing vote requirements for the various proposals.

- The four nominees for director receiving the most votes will be elected. Abstentions and instructions to withhold authority to vote for one or more of the nominees will result in those nominees receiving fewer votes but will not count as votes against a nominee.

- The appointment of principal independent auditors will be approved if the votes cast for the proposal exceed those cast against the proposal. Abstentions will not be counted either for or against the proposal.

- The shareholder proposals will be approved if the votes cast for the proposal exceed those cast against the proposal. Abstentions and broker nonvotes will not be counted either for or against the proposal.

Broker nonvotes. If your shares are held by a broker, the broker will ask you how you want your shares to be voted. If you give the broker instructions, your shares will be voted as you direct. If you do not give instructions, one of two things can happen, depending on the type of proposal. For the election of directors and the ratification of auditors, the

broker may vote your shares in its discretion. For the shareholder proposals, the broker may not vote your shares at all. When that happens, it is called a broker nonvote.

How do I vote by proxy?

If you are a shareholder of record, you may vote your proxy by any one of the following methods.

By mail. Sign and date each proxy card you receive and return it in the prepaid envelope. Sign your name exactly as it appears on the proxy. If you are signing in a representative capacity (for example, as an attorney-in-fact, executor, administrator, guardian, trustee, or the officer or agent of a corporation or partnership), please indicate your name and your title or capacity. If the stock is held in custody for a minor (for example, under the Uniform Transfers to Minors Act), the custodian should sign, not the minor.

If the stock is held in joint ownership, one owner may sign on behalf of all owners. If you return your signed proxy but do not indicate your voting preferences, we will vote on your behalf for the election of the four nominees for director listed below, for the ratification of the appointment of the independent auditors, and against the shareholder proposals.

Note that if you previously elected to receive these materials electronically, you did not receive a proxy card. If you wish to vote by mail, rather than by telephone or on the Internet as discussed below, you may request paper copies of these materials, including a proxy card, by calling 317-433-5112. Please make sure you give us the control number from the e-mail message that you received notifying you of the electronic availability of these materials, along with your name and mailing address.

By telephone. Shareholders in the United States, Puerto Rico, and Canada may vote by telephone by following the instructions on the enclosed proxy card or, if you received these materials electronically, by following the instructions in the e-mail message that notified you of their availability. Voting by telephone has the same effect as voting by mail. If you vote by telephone, do not return your proxy card. Telephone voting will be available until 11:59 p.m. EDT, April 23, 2006.

By Internet. You may vote online at www.proxyvote.com. Follow the instructions on the enclosed proxy card or, if you received these materials electronically, the instructions in the e-mail message that notified you of their availability. Voting on the Internet has the same effect as voting by mail. If you vote on the Internet, do not return your proxy card. Internet voting will be available until 11:59 p.m. EDT, April 23, 2006.

You have the right to revoke your proxy at any time before the meeting by (1) notifying the company's secretary in writing or (2) delivering a later-dated proxy by telephone, on the Internet, or in writing. If you are a shareholder of record, you may also revoke your proxy by voting in person at the meeting.

How do I vote shares that are held by my broker?

If you have shares held by a broker or other nominee, you may instruct your broker or other nominee to vote your shares by following instructions that the broker or nominee provides for you. Most brokers offer voting by mail, telephone, and on the Internet.

How do I vote in person?

If you are a shareholder of record, you may vote your shares in person at the meeting. However, we encourage you to vote by proxy card, by telephone, or on the Internet even if you plan to attend the meeting.

How do I vote my shares in the 401(k) plan?

You may instruct the plan trustee on how to vote your shares in the 401(k) plan by mail, by telephone, or on the Internet as described above, except that, if you vote by mail, the card that you use will be a voting instruction card rather than a proxy card.

How many shares in the 401(k) plan can I vote?

You may vote all the shares allocated to your account on the record date. In addition, unless you decline, your vote will also apply to a proportionate number of other shares held in the 401(k) plan for which voting directions are not received. These undirected shares include:

- shares credited to the accounts of participants who do not return their voting instructions (except for a small number of shares from a prior stock ownership plan, which can be voted only on the directions of the participants to whose accounts the shares are credited)

- shares held in the plan that are not yet credited to individual participants' accounts.

All participants are named fiduciaries under the terms of the 401(k) plan and under the Employee Retirement Income Security Act (ERISA) for the limited purpose of voting shares credited to their accounts and the portion of undirected shares to which their vote applies. Under ERISA, fiduciaries are required to act prudently in making voting decisions.

If you do not want to have your vote applied to the undirected shares, you should check the box marked "I decline." Otherwise, the trustee will automatically apply your voting preferences to the undirected shares proportionally with all other participants who elected to have their votes applied in this manner.

What happens if I do not vote my 401(k) plan shares?

Your shares will be voted by other plan participants who have elected to have their voting preferences applied proportionally to all shares for which voting instructions are not otherwise received.

What does it mean if I receive more than one proxy card?

It means that you hold shares in more than one account. To ensure that all your shares are voted, sign and return each card. Alternatively, if you vote by telephone or on the Internet, you will need to vote once for each proxy card and voting instruction card you receive.

Who tabulates the votes?

The votes are tabulated by an independent inspector of election, IVS Associates, Inc.

What should I do if I want to attend the annual meeting?

All shareholders as of the record date may attend by presenting the admission ticket that appears at the end of this proxy statement. Please fill it out and bring it with you to the meeting. The meeting will be held at the Lilly Center Auditorium. Please use the Lilly Center entrance to the south of the fountain at the intersection of Delaware and McCarty streets. You will need to pass through security, including a metal detector. Present your ticket to the usher at the meeting.

Parking will be available on a first-come, first-served basis in the garage indicated on the map on page 37. If you have questions about admittance or parking, you may call 317-433-5112.

Will the annual meeting be available on the Internet?

The annual meeting will be broadcast live via webcast on the company's website. To join the live webcast, go to www.lilly.com and click on the annual meeting link that appears on the home page. The webcast will be available in both the Windows Media Player and RealPlayer® formats. It will be available for replay on the Lilly website until May 24, 2006.

How do I contact the board of directors?

You can send written communications to one or more members of the board, addressed to:

Presiding Director, Board of Directors

Eli Lilly and Company

c/o Corporate Secretary

Lilly Corporate Center

Indianapolis, Indiana 46285

All such communications will be forwarded to the relevant director(s), except for solicitations or other matters unrelated to the company.

How do I submit a shareholder proposal for the 2007 annual meeting?

The company's 2007 annual meeting is scheduled for April 16, 2007. If a shareholder wishes to have a proposal considered for inclusion in next year's proxy statement, he or she must submit the proposal in writing so that we receive it by November 13, 2006. Proposals should be addressed to the company's corporate secretary, Lilly Corporate Center, Indianapolis, Indiana 46285. In addition, the company's bylaws provide that any shareholder wishing to propose any other business at the annual meeting must give the company written notice by November 13, 2006. That notice must provide certain other information as described in the bylaws. Copies of the bylaws are available online at <http://investor.lilly.com/bylaws.cfm>.

Does the company offer an opportunity to receive future proxy materials electronically?

Yes. If you are a shareholder of record or a member of the 401(k) plan, you may, if you wish, receive future proxy statements and annual reports online. If you elect this feature, you will receive an e-mail message notifying you when the materials are available along with a web address for viewing the materials and instructions for voting by telephone or on the Internet. If you have more than one account, you may receive separate e-mail notifications for each account.

You may sign up for electronic delivery in two ways:

If you vote online as described above, you may sign up for electronic delivery at that time.

You may sign up at any time by visiting <http://proxyonline.lilly.com>.

If you received these materials electronically, you do not need to do anything to continue receiving materials electronically in the future.

If you hold your shares in a brokerage account, you may also have the opportunity to receive proxy materials electronically. Please follow the instructions of your broker.

What are the benefits of electronic delivery?

Electronic delivery reduces the company's printing and mailing costs. It is also a convenient way for you to receive your proxy materials and makes it easy to vote your shares online. If you have shares in more than one account, it is an easy way to avoid receiving duplicate copies of proxy materials.

What are the costs of electronic delivery?

The company charges nothing for electronic delivery. You may, of course, incur the usual expenses associated with Internet access, such as telephone charges or charges from your Internet service provider.

May I change my mind later?

Yes. You may discontinue electronic delivery at any time. For more information, call 317-433-5112.

What is householding ?

We have adopted householding, a procedure under which shareholders of record who have the same address and last name and do not receive proxy materials electronically will receive only one copy of our annual report and proxy statement unless one or more of these shareholders notifies us that they wish to continue receiving individual copies. This procedure saves printing and postage costs by reducing duplicative mailings.

Shareholders who participate in householding will continue to receive separate proxy cards. Householding will not affect dividend check mailings.

Beneficial shareholders can request information about householding from their banks, brokers, or other holders of record.

What if I want to receive a separate copy of the annual report and proxy statement?

If you participate in householding and wish to receive a separate copy of the 2005 annual report and 2006 proxy statement, or if you wish to receive separate copies of future annual reports and proxy statements, please call us at 317-433-5112 or write to: Household Department, 51 Mercedes Way, Edgewood, New York 11717. We will deliver the requested documents to you promptly upon your request.

Board of Directors

Directors' Biographies

Class of 2006

The following four directors' terms will expire at this year's annual meeting. Each of these directors has been nominated and is standing for election to serve another term that will expire in 2009. See page 29 of this proxy statement for more information. Charles E. Golden is also a member of the class of 2006. In light of his retirement from the company effective April 30, 2006, he is not standing for re-election.

Martin S. Feldstein, Ph.D.

President and Chief Executive Officer, National Bureau of Economic Research, and George F. Baker Professor of Economics, Harvard University

Director since 2002 Age 66

Dr. Feldstein is president and chief executive officer of the National Bureau of Economic Research and the George F. Baker Professor of Economics at Harvard University. He became an assistant professor at Harvard in 1967 and an associate professor in 1968. From 1982 through 1984, he served as chairman of the Council of Economic Advisers and President Ronald Reagan's chief economic adviser. He is a member of the American Philosophical Society, a corresponding fellow of the British Academy, a fellow of the Econometric Society, and a fellow of the National Association for Business Economics. Dr. Feldstein is a member of the executive committee of the Trilateral Commission and a director of the Council on Foreign Relations; American International Group, Inc.; Economic Studies, Inc.; and HCA Inc. He is a member of the American Academy of Arts and Sciences and past president of the American Economic Association.

J. Erik Fyrwald

Group Vice President, DuPont Agriculture & Nutrition

Director since 2005 Age 46

Mr. Fyrwald has been group vice president of DuPont Agriculture & Nutrition since 2003. He was previously vice president and general manager of DuPont's nutrition and health businesses, which included The Solae Company, DuPont Qualicon, Liqui-Box, and DuPont Food Industry Solutions. Mr. Fyrwald joined DuPont in 1981 as a production engineer, and held a variety of sales and management positions in a number of areas. In 1990, he became the leader of the DuPont Engineering Polymers and DuPont Butacite® businesses for the Asia Pacific region, a position he held until 1994. He was named leader of the DuPont Nylon Plastics business for the Americas until 1996, when he became head of global sales and marketing for engineering polymers. In 1998, he was appointed vice president of corporate plans and business development and then vice president of e-commerce. Mr. Fyrwald serves on the boards of the Biotechnology Industry Organization (BIO); CropLife International President's Advisory Group; Des Moines Art Center; Farm Foundation; 8th Continent L.L.C.; and The Solae Company. He has been serving under interim election

since November 2005.

Ellen R. Marram

President, The Barnegat Group LLC

Director since Age 59
2002

Ms. Marram is the president of The Barnegat Group LLC, a firm that provides business advisory services. She was a managing director at North Castle Partners, LLC from 2000 to 2005 and is currently an advisor to the firm. Prior to joining North Castle, she served as the chief executive officer of a start-up B2B exchange for the food and beverage industry. From 1993 through 1998, Ms. Marram was president and chief executive officer of Tropicana and the Tropicana Beverage Group. From 1988 to 1993, she was president and chief executive officer of the Nabisco Biscuit Company, an operating unit of Nabisco, Inc.; from 1987 to 1988, was president of Nabisco's Grocery Division; and from 1970 to 1986, held a series of marketing positions at Nabisco/Standard Brands, Johnson & Johnson, and Lever Brothers.

Ms. Marram is a member of the board of directors of Ford Motor Company and The New York Times Company as well as several private companies. She serves on the boards of The New York-Presbyterian Hospital, Lincoln Center Theater, Families and Work Institute, and Citymeals-on-Wheels.

Sidney Taurel

Chairman of the Board and Chief Executive Officer

Director since Age 57
1991

Mr. Taurel has been the company's chief executive officer since July 1998 and chairman of the board since January 1999. He also served as president from February 1996 through September 2005. He joined the company in 1971 and has held management positions in the company's international operations based in São Paulo, Vienna, Paris, and London. Mr. Taurel served as president of Eli Lilly International Corporation from 1986 to 1991, executive vice president of the pharmaceutical division from 1991 to 1993, and executive vice president of the company from 1993 until 1996. He is a member

of the boards of IBM Corporation and The McGraw-Hill Companies, Inc. He is also a member of the executive committee of the board of directors of Pharmaceutical Research and Manufacturers of America (PhRMA), a member of the board of overseers of the Columbia Business School, a trustee at the Indianapolis Museum of Art, a director of the RCA Tennis Championships, and a member of The Business Council and The Business Roundtable. In 2001, Mr. Taurel became a chevalier of the French Legion of Honor. He was appointed in February 2003 to the President's Export Council.

Class of 2007

The following four directors will continue in office until 2007.

Sir Winfried Bischoff

Chairman, Citigroup Europe

Director since Age 64
2000

Sir Winfried Bischoff has served as chairman, Citigroup Europe, since April 2000. From 1995 to 2000, he was chairman of Schroders, plc. He joined the Schroder Group in 1966 and held a number of positions there, including chairman of J. Henry Schroder Co. and group chief executive of Schroders, plc. He is a nonexecutive director of The McGraw-Hill Companies, Inc., and Land Securities plc.

J. Michael Cook

Retired Chairman and Chief Executive Officer, Deloitte and Touche LLP

Director since Age 63
2005

Mr. Cook served as chairman and chief executive officer of Deloitte and Touche, LLP from 1989 until his retirement in 1999. He joined Deloitte, Haskins & Sells in 1964 and served as chairman and chief executive officer from 1986 through 1989. Mr. Cook is a member of the Advisory Council of the Public Company Accounting Oversight Board and is a trustee of The Scripps Research Institute. He serves on the boards of Comcast Corporation, The Dow Chemical Company and International Flavors & Fragrances Inc. He is chairman of the Accountability Advisory Council to the Comptroller General of the United States. He was a member of the National Association of Corporate Directors Blue Ribbon Panel on Corporate Governance and was named the 62nd member of the Accounting Hall of Fame in 1999. He is president of the Institute of Outstanding Directors.

Franklyn G. Prendergast, M.D., Ph.D.

Edmond and Marion Guggenheim Professor of Biochemistry and Molecular Biology and Professor of Molecular Pharmacology and Experimental Therapeutics, Mayo Medical School, and Director, Mayo Clinic Cancer Center

Age 60

Director since
1995

Dr. Prendergast is the Edmond and Marion Guggenheim Professor of Biochemistry and Molecular Biology and Professor of Molecular Pharmacology and Experimental Therapeutics at Mayo Medical School and the director of the Mayo Clinic Cancer Center. He has held several other teaching positions at the Mayo Medical School since 1975. Dr. Prendergast serves on the board of trustees of the Mayo Foundation and the Mayo Clinic Board of Governors.

Kathi P. Seifert

Retired Executive Vice President, Kimberly-Clark Corporation

Director since Age 56
1995

Ms. Seifert served as executive vice president for Kimberly-Clark Corporation until June 2004. She joined Kimberly-Clark in 1978 and served in several capacities in connection with both the domestic and international consumer products businesses, most recently leading the team that develops and manages global plans for branding and product positioning, R&D programs, and capital investment for personal care products. She also oversaw Kimberly-Clark's U.S. and Canadian sales forces. Prior to joining Kimberly-Clark, Ms. Seifert held management positions at Procter & Gamble, Beatrice Foods, and Fort Howard Paper Company. She is chair of Pinnacle Perspectives, LLC. Ms. Seifert serves on the boards of Albertsons, Inc.; Revlon, Inc.; Appleton Papers Inc.; the U.S. Fund for UNICEF; and the Fox Cities Performing Arts Center.

Class of 2008

The following four directors will continue in office until 2008.

George M.C. Fisher

Retired Chairman of the Board and Chief Executive Officer, Eastman Kodak Company

Director since Age 65
2000

Mr. Fisher served as chairman of the board of Eastman Kodak Company from 1993 to December 2000. He also served as chief executive officer from 1993 to January 2000 and as president from 1993 until 1996. Prior to joining Kodak, he was an executive officer of Motorola, Inc., serving as chairman and chief executive officer from 1990 to October 1993, and president and chief executive officer from 1988 to 1990. Mr. Fisher is chairman of PanAmSat Corporation, a senior advisor for Kohlberg Kravis

Roberts & Company, and a director of General Motors Corporation and Visant Corporation. He is a member of The Business Council and was chairman of the National Academy of Engineering from 2000 to 2004.

Alfred G. Gilman, M.D., Ph.D.

Dean, The University of Texas Southwestern Medical School and Regental Professor of Pharmacology, The University of Texas Southwestern Medical Center

Director since Age 64
1995

Dr. Gilman has served as dean of The University of Texas Southwestern Medical School since 2005 and professor of pharmacology at The University of Texas Southwestern Medical Center since 1981. He holds the Raymond and Ellen Willie Distinguished Chair in Molecular Neuropharmacology, the Nadine and Tom Craddick Distinguished Chair in Medical Science, and the Atticus James Gill, M.D. Chair in Medical Science at the university and was named a regental professor in 1995. Dr. Gilman was on the faculty of the University of Virginia School of Medicine from 1971 until 1981 and was named a professor of pharmacology there in 1977. He is a director of Regeneron Pharmaceuticals, Inc. Dr. Gilman was a recipient of the Nobel Prize in Physiology or Medicine in 1994.

Karen N. Horn, Ph.D.

Retired President, Private Client Services, and Managing Director, Marsh, Inc.

Director since Age 62
1987

Ms. Horn served as president, Private Client Services, and managing director of Marsh, Inc., a subsidiary of MMC, from 1999 until her retirement in 2003. Prior to joining Marsh, she was senior managing director and head of international private banking at Bankers Trust Company; chair and chief executive officer, Bank One, Cleveland, N.A.; president of the Federal Reserve Bank of Cleveland; treasurer of Bell of Pennsylvania; and vice president of First National Bank of Boston. Ms. Horn serves as director of T. Rowe Price Mutual Funds; The U.S. Russia Investment Fund, a presidential appointment; and Simon Property Group, Inc. Ms. Horn has been senior managing director, Brock Capital Group since 2004.

John C. Lechleiter, Ph.D.

President and Chief Operating Officer

Director since Age 52
2005

Dr. Lechleiter has served as president and chief operating officer of the company since October 2005. He joined Lilly in 1979 as a senior organic chemist and has held management positions in England and the U.S. He was

named vice president of pharmaceutical product development in 1993 and vice president of regulatory affairs in 1994. In 1996, he was named vice president for development and regulatory affairs. Dr. Lechleiter became senior vice president of pharmaceutical products in 1998, and executive vice president, pharmaceutical products and corporate development in 2001. He was named executive vice president, pharmaceutical operations in 2004. He is a member of the American Chemical Society. In 2004, Dr. Lechleiter was appointed to the Visiting Committee of Harvard Business School and to the Health Policy and Management Executive Council of the Harvard School of Public Health. He also serves as a member of the Board of Trustees of Xavier University (Cincinnati, Ohio). In addition, he serves as a distinguished advisor to The Children's Museum of Indianapolis and as a member of the Dean's Advisory Board at the Indiana University School of Medicine. Dr. Lechleiter has been serving under interim election since October 2005.

Highlights of the Company's Corporate Governance Guidelines

The board of directors has established guidelines that it follows in matters of corporate governance. The following summary provides highlights of those guidelines. A complete copy of the guidelines is available online at <http://investor.lilly.com/guidelines.cfm> or in paper form upon request to the company's corporate secretary.

I. Role of the Board

The directors are elected by the shareholders to oversee the actions and results of the company's management. Their responsibilities include:

- providing general oversight of the business

- approving corporate strategy and major management initiatives

- providing oversight of legal and ethical conduct

- selecting, compensating, and evaluating directors

- evaluating board processes and performance

- selecting, compensating, evaluating, and, when necessary, replacing the chief executive officer, and compensating other executive officers

- ensuring that a succession plan is in place for all senior executives.

II. Composition of the Board

Mix of Independent Directors and Officer-Directors

There should always be a substantial majority (75 percent or more) of independent directors. The chief executive officer should be a board member. Other officers may, from time to time, be board members, but no officer other than the chief executive officer should expect to be elected to the board by virtue of his or her office.

Selection of Director Candidates

The board is responsible for selecting candidates for board membership and for establishing the criteria to be used in identifying potential candidates. The board delegates the screening process to the directors and corporate governance committee. For more information on the director nomination process, including the current selection criteria, see Directors and Corporate Governance Committee Matters on page 16.

Independence Determinations

The board annually determines the independence of directors based on a review by the directors and corporate governance committee. No director is considered independent unless the board has determined that he or she has no material relationship with the company, either directly or as a partner, shareholder, or officer of an organization that has a material relationship with the company. Material relationships can include commercial, industrial, banking, consulting, legal, accounting, charitable, and familial relationships, among others. To evaluate the materiality of any such relationship, the board has adopted categorical independence standards consistent with the revised New York Stock Exchange listing guidelines adopted in November 2003 and amended in November 2004.

Specifically, a director is not considered independent if (i) the director or an immediate family member is a current partner of Lilly's independent auditor (currently Ernst & Young LLP); (ii) the director is a current employee of such firm; (iii) the director has an immediate family member who is a current employee of such firm and who participates in the firm's audit, assurance, or tax compliance (but not tax planning) practice; or (iv) the director or immediate family member was within the last three years (but is no longer) a partner or employee of such firm and personally worked on the listed company's audit within that time.

In addition, a director is not considered independent if any of the following relationships existed within the previous three years:

- a director who is an employee of Lilly, or whose immediate family member is an executive officer of Lilly.

- Temporary service by an independent director as interim chairman or chief executive officer will not disqualify

the director from being independent following completion of that service.

a director who receives any direct compensation from Lilly other than the director's normal director compensation, or whose immediate family member receives more than \$100,000 per year in direct compensation from Lilly other than for service as a non-executive employee.

a director who is employed (or whose immediate family member is employed as an executive officer) by another company where any Lilly executive officer serves on that company's compensation committee.

a director who is employed by, who is a 10 percent shareholder of, or whose immediate family member is an executive officer of a company that makes payments to or receives payments from Lilly for property or services that exceed the greater of \$1 million or 2 percent of that company's gross revenues in a single fiscal year.

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a director who is an executive officer of a nonprofit organization that receives grants or contributions from Lilly in a single fiscal year exceeding the greater of \$1 million or 2 percent of that organization's gross revenues in a single fiscal year.

Members of the audit, compensation, and directors and corporate governance committees must meet all applicable independence tests of the New York Stock Exchange, Securities and Exchange Commission, and Internal Revenue Service.

The board has determined that all 10 of the nonemployee directors listed on pages 7-9 are independent pursuant to the above criteria and that the board committee members meet all applicable independence standards.

Director Tenure

Subject to the company's charter documents, the governance guidelines establish the following expectations for director tenure:

A company officer-director, including the chief executive officer, will resign from the board at the time he or she retires or otherwise ceases to be an active employee of the company.

Nonemployee directors will retire from the board not later than the annual meeting of shareholders that follows their seventy-second birthday.

Directors may stand for reelection even though the board's retirement policy would prevent them from completing a full three-year term.

A nonemployee director who retires or changes principal job responsibilities will offer to resign from the board. The directors and corporate governance committee will assess the situation and recommend to the board whether to accept the resignation.

Voting for Directors

In an uncontested election, any nominee for director who receives a greater number of votes withheld from his or her election than votes for such election (a majority withheld vote) shall promptly tender his or her resignation following certification of the shareholder vote.

The directors and corporate governance committee shall consider the resignation offer and recommend to the board whether to accept it. The board will act on the committee's recommendation within 90 days following the shareholder meeting. Board action on the matter will require the approval of a majority of the independent directors.

The company will disclose the board's decision on a Form 8-K furnished to the Securities and Exchange Commission within four business days after the decision, including a full explanation of the process by which the decision was reached and, if applicable, the reasons why the board rejected the directors' resignation. If the resignation is accepted, the directors and corporate governance committee will recommend to the board whether to fill the vacancy or reduce the size of the board.

Any director who tenders his or her resignation pursuant to this provision shall not participate in the committee or board deliberations regarding whether to accept the resignation offer.

If each member of the directors and corporate governance committee receives a majority withheld vote at the same election, then the independent directors who did not receive a majority withheld vote shall appoint a committee amongst themselves to consider the resignation offers and recommend to the board whether to accept them.

III. Director Compensation and Equity Ownership

The directors and corporate governance committee annually reviews board compensation. Any recommendations for changes are made to the full board by the committee.

Directors should hold meaningful equity ownership positions in the company; accordingly, a significant portion of overall director compensation is in the form of company equity.

IV. Key Responsibilities of the Board

Selection of Chairman and Chief Executive Officer; Succession Planning

The board customarily combines the roles of chairman and chief executive officer, believing this generally provides the most efficient and effective leadership model for the company. The board anticipates that, in certain occasional

circumstances, and particularly during relatively short periods of leadership transition, these roles could be assigned to two different persons for a period of time. The presiding director recommends to the board an appropriate process by which a new chairman and chief executive officer will be selected.

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The independent directors are responsible for overseeing succession and management development programs for senior leadership. The chief executive officer develops and maintains a process for advising the board on succession planning for the chief executive officer and other key leadership positions. He or she reviews this plan with the independent directors at least annually.

Evaluation of Chief Executive Officer

The chair of the compensation committee leads the independent directors annually in assessing the performance of the chief executive officer. The results of this review are discussed with the chief executive officer and considered by the compensation committee in establishing his or her compensation for the next year.

Corporate Strategy

Once each year, the board devotes an extended meeting to an update from management regarding the strategic issues and opportunities facing the company, allowing the board an opportunity to provide direction for the corporate strategic plan. Throughout the year, significant corporate strategy decisions are brought to the board for approval.

Code of Ethics

The board approved the company's code of ethics, which complies with the requirements of the New York Stock Exchange and Securities and Exchange Commission. This code is set forth in:

The Red Book, a comprehensive code of ethical and legal business conduct applicable to all employees worldwide and to our board of directors

the company's Code of Ethical Conduct for Lilly Financial Management, a supplemental code for our chief executive officer, chief operating officer, and all members of financial management that recognizes the unique responsibilities of those individuals in assuring proper accounting, financial reporting, internal controls, and financial stewardship.

Both documents are available online at http://investor.lilly.com/code_business_conduct.cfm or in paper form upon request to the company's corporate secretary.

The audit committee and public policy and compliance committee assist in the board's oversight of compliance programs with respect to matters covered in the code of ethics.

V. Functioning of the Board

Executive Session of Directors

The independent directors meet alone in executive session at every regularly scheduled board meeting. In addition, at least twice a year, the independent directors meet in executive session with the chief executive officer.

Presiding Director

The board appoints a presiding director from among the independent directors (currently Ms. Horn). The presiding director:

leads the board's process for selecting and evaluating the chief executive officer;

presides at all meetings of the board at which the chairman is not present, including executive sessions of the independent directors unless the directors decide that, due to the subject matter of the session, another independent director should preside;

serves as a liaison between the chairman and the independent directors;

generally approves information sent to the board and meeting agendas and schedules; and

has the authority to call meetings of the independent directors.

Conflicts of Interest

Occasionally a director's business or personal relationships may give rise to an interest that conflicts, or appears to conflict, with the interests of the company. Directors must disclose to the company all relationships that create a conflict or an appearance of a conflict. The board, after consultation with counsel, takes appropriate steps to ensure that all directors voting on an issue are disinterested. In appropriate cases, the affected director will be excused from

discussions on the issue.

To avoid any conflict or appearance of a conflict, board decisions on certain matters of corporate governance are made solely by the independent directors. These include executive compensation and the selection, evaluation, and removal of the chief executive officer.

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Orientation and Continuing Education

A comprehensive orientation process is in place for new directors. In addition, directors receive ongoing continuing education through educational sessions at meetings, the annual strategy retreat, and periodic mailings between meetings. We hold periodic mandatory training sessions for the audit committee, to which other directors and executive officers are invited. We also afford directors the opportunity to attend external director education programs.

Director Access to Management and Independent Advisers

Independent directors have direct access to members of management whenever they deem it necessary. The independent directors and the committees are also free to retain their own independent advisers, at company expense, whenever they feel it would be desirable to do so. In accordance with New York Stock Exchange listing standards, the audit, compensation, and directors and corporate governance committees have sole authority to retain independent advisers to their respective committees.

Assessment of Board Processes and Performance

The directors and corporate governance committee annually assesses the performance of the board, its committees, and board processes based on inputs from all directors. The committee also considers the contributions of individual directors at least every three years when considering whether to recommend nominating the director to a new three-year term.

VI. Board Committees

Number, Structure, and Independence

The duties and membership of the six board-appointed committees are described below. Only independent directors may serve on the audit, compensation, directors and corporate governance, and public policy and compliance committees. Only independent directors may chair any committee.

Committee membership and selection of committee chairs are recommended to the board by the directors and corporate governance committee after consulting the chairman of the board and after considering the desires of the board members.

Functioning of Committees

Each committee reviews and approves its own charter annually, and the directors and corporate governance committee reviews and approves all committee charters annually. The board may form new committees or disband a current committee (except the audit, compensation, and directors and corporate governance committees) as it deems appropriate. The chair of each committee determines the frequency and agenda of committee meetings.

All six committee charters are available online at <http://investor.lilly.com/board-committees.cfm> or in paper form upon request to the company's corporate secretary.

Committees of the Board of Directors

Audit Committee

The duties of the audit committee are described in the audit committee report found on page 17 of this proxy statement.

Directors and Corporate Governance Committee

The duties of the directors and corporate governance committee are described on page 16.

Compensation Committee

evaluates and establishes compensation for executive officers

oversees the deferred compensation plan, the company's management stock plans, and other management incentive programs.

The compensation committee report is shown on pages 19-22 of this proxy statement.

Public Policy and Compliance Committee

oversees the processes by which the company conducts its business so that the company will do so in a manner that complies with laws and regulations and reflects the highest standards of integrity

reviews and makes recommendations regarding policies, practices, and procedures of the company that relate to public policy and social, political, and economic issues that may affect the company.

Finance Committee

reviews and makes recommendations regarding capital structure and strategies, including dividends, stock repurchases, capital expenditures, financings and borrowings, and complex business development projects.

Science and Technology Committee

reviews and makes recommendations regarding the company's strategic research goals and objectives

reviews new developments, technologies, and trends in pharmaceutical research and development.

Membership and Meetings of the Board and Its Committees

In 2005, each director attended more than 80 percent of the total number of meetings of the board and the committees on which he or she serves. In addition, all board members are expected to attend the annual meetings of shareholders, and all attended in 2005. Current committee membership and the number of meetings of the full board and each committee in 2005 are shown in the table below.

	Board	Audit	Compensation	Directors and Corporate Governance	Finance	Public Policy and Compliance	Science and Technology
Sir Winfried Bischoff	Member	Chair			Member		
Mr. Cook	Member	Member	Member		Member		
Dr. Feldstein	Member	Member			Chair	Member	
Mr. Fisher	Member		Member	Chair			Member
Mr. Fyrwald ¹	Member		Member				Member
Dr. Gilman	Member					Member	Member
Mr. Golden	Member				Member		
Ms. Horn	Member		Chair	Member			
Dr. Lechleiter ²	Member						Member
Ms. Marram	Member		Member	Member			
Dr. Prendergast	Member	Member				Member	Chair
Ms. Seifert	Member	Member			Member	Chair	
Mr. Taurel	Chair						

Number of 2005 7	12	3	3	4	6	3
Meetings						

¹ Mr. Fyrwald joined the board in November 2005.

² Dr. Lechleiter joined the board in October 2005.

Directors Compensation

Directors who are employees receive no additional compensation for serving on the board or its committees.

In 2005, we provided the following annual compensation to directors who are not employees:

	Total	Fees Earned or Paid in Cash	Stock Awards	Option Awards	Non-Stock Incentive Plan Compensation	All Other Compensation (1)
Name	(\$)	(\$)	(\$)	(\$)	(\$)	(\$)
Sir Winfried Bischoff	178,145	96,200	75,758	0	0	6,187
Mr. Cook	147,405	70,050	75,758	0	0	1,597
Dr. Feldstein	156,764	76,555	75,758	0	0	4,451
Mr. Fisher	161,969					