

## Morgan Stanley

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Technical Director—File Reference No. 1530-100 Financial Accounting Standards Board 401 Merritt 7 PO Box 5116 Norwalk, CT 06856-5116

Re: Proposed Statement 133 Implementation No. E23, "Issues Involving the Application of the Shortcut Method under Paragraph 68"

Dear Technical Director:

Morgan Stanley appreciates the opportunity to comment on the Proposed Statement 133 Implementation No. E23, "Issues Involving the Application of the Shortcut Method under Paragraph 68" (the "proposed Implementation Issue").

While Morgan Stanley supports the Board's objective to improve financial reporting related to the shortcut method and to increase comparability in the financial statements, we have concerns regarding the proposed implementation guidance specifically in regards to the proposed guidance governing the application of the shortcut method to a fair value hedging relationship that begins subsequent to the initial recognition of the hedged item.

We would like to note that we have recently ceased our short cut hedge programs and currently are only applying hedge accounting under the "long haul" method. Our decision was made in part due to the ever-evolving interpretations of the short cut method in general, and in particular, the interpretations of the intent of paragraph 68(e) with regards to circumstances in hedging relationship that are considered "not typical" or "invalidate the assumption of no ineffectiveness."

Although we are no longer applying the short cut method, we do strongly agree with the alternative views expressed by the three dissenting Board members in that we do not believe that FAS 133 currently requires that a condition of the shortcut method is that the fair value of the hedged item has to equal its principal amount (which disqualifies hedge transactions that are entered into after the initial recognition of the hedged instrument) and that existing guidance within FAS 133 supports this view (specifically paragraph 68b which explicitly requires the swap to have a fair value of zero at inception, but does not explicitly require that the hedged item be at par, footnotes to paragraphs 115 and 134

which state that the trade date of the swap and the borrowing date of the debt need not match for the assumption of no ineffectiveness to be appropriate, and Derivatives Implementation ("DIG") Issue J9, "Use of the Shortcut Method in Transition Adjustment and Upon Initial Adoption," which describes the application of the shortcut method to a hedged item that existed prior to adoption of FAS 133 so long as the fair value of the swap was zero at the date of adoption).

If the Board were to amend FAS 133 to prohibit the application of the shortcut method to these transactions, companies would need to develop or acquire the necessary systems to properly re-designate and account for their hedges under the more onerous "long-haul" approach. Given our experiences in doing just that, we feel strongly that the proposed effective date does not allow enough time for companies to comply with the requirements to maintain hedge accounting under the long-haul approach.

We are aware that the Board has added a project to its agenda to address hedging activities in FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities, and is working on approaches that may do away with the shortcut method altogether. Rather than move forward with the proposed Implementation Issue, we would urge the Board to consider addressing the shortcut method in conjunction with the broader project to address hedge accounting activities.

If the Board decides to issue the proposed Implementation Guidance, we recommend the Board consider either allowing companies to "grandfather" all hedging relationships that meet the current requirements of the shortcut method under paragraph 68, and apply the Implementation Guidance for hedge transactions that are entered into after initial issuance or purchase on a prospective basis, or consider delaying the effective date to give companies enough time to comply with the more onerous requirements of the long-haul method in order to retain hedge accounting for their transactions.

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We would be pleased to discuss our comments with the Board members of the FASB staff at your convenience. Please contact Esther Mills at (212) 276-4364 or me at (212) 276-7716 with any questions or comments.

Yours sincerely,

/s/ Greg Sigrist
Managing Director