



September 20, 2007

Russell G. Golden  
Director of Technical Application & Implementation Activities  
FASB  
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**File Reference: Proposed Issue E23**

Dear Mr. Golden:

We appreciate the opportunity to comment on the Financial Accounting Standards Board's (the "FASB" or "the Board") Exposure Draft of DIG Issue E23, *Hedging—General: Issues Involving the Application of the Shortcut Method under Paragraph 68* ("DIG Issue E23" or "the Exposure Draft").

We agree with the FASB that certain practice issues exist relative to the application of the shortcut method and, more generally, the application of hedge accounting under Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities* ("FAS 133"). We support the FASB's goal of improving financial reporting related to the shortcut method to increase comparability in financial statements. However, we believe the elimination of the use of the shortcut method for late hedging, in its entirety, represents a major change in how FAS 133 is currently applied to hedges and may have a detrimental effect on how Exelon and other companies manage the costs and risks of their debt portfolios. We do not believe that FAS 133 currently requires the fair value of the hedged item to be equal to its principal amount at the hedging date as a condition for using the shortcut method. Amending FAS 133 to explicitly include this requirement through the issuance of the Exposure Draft would result in increased costs and bookkeeping requirements due to periodic effectiveness testing that would be required for late hedges. We do not believe that these increased costs are justified for this narrow set of highly effective, extremely common transactions.

Exelon Corporation (Exelon) historically has used fixed-to-floating interest rate swaps for the purpose of efficiently managing the fixed-floating mix of our debt portfolio. We execute these swaps in order to achieve and maintain our targeted mix of fixed-floating rate debt in a cost-effective and flexible manner. Our historical use of these fixed-to-floating interest rate swaps has been infrequent. When we do enter into these swaps, we manage the risk of interest rate uncertainty and bank credit risk (both of which have a greater degree of uncertainty when spread over a longer term) by entering into hedges subsequent to the issuance of the fixed-rate debt instrument. That is, rather than enter into hedges at the same time as the issuance of the fixed-rate debt instruments when their term is long and uncertainty is greater, we enter into hedges as they get closer to maturity (typically 5-8 years prior to final maturity). These transactions would be considered "late

hedges” as contemplated by the Exposure Draft. We believe these late hedges to be highly effective trades, and we generally do not intend to settle our hedges prior to the end of their terms. However, Exelon and other registrants need to retain the financial flexibility to settle these hedges early if business conditions necessitate.

We have historically designated these fixed-to-floating interest rate swaps as fair value hedges and evaluate them pursuant to the shortcut method as we believe all requirements of Paragraph 68 of FAS 133 have been met for these late hedges. We believe that changes in the fair value of the swap will be highly effective in offsetting subsequent changes in the fair value of debt attributable to changes in interest rates. Assuming that other criteria of Paragraph 68 of FAS 133 are met, the underlying cash flows and economics of the hedging relationship are represented just as faithfully for these late hedges as for other shortcut hedges. Shortcut method treatment is faithful to the economics of these trades, as pre-hedge gain or loss on the hedged debt instrument is reflected in the swap economics and recognized via the swap accruals over the life of the hedging relationship.

Paragraphs 115 and 134 of FAS 133 currently state that the trade and settlement date are not required to match in order for a no-ineffectiveness conclusion to be appropriate. In addition, we do not believe that FAS 133 currently requires the fair value of a hedged item to be equal to its principal amount at the hedging date. Therefore, the Exposure Draft is inconsistent with FAS 133 and would be a significant change in GAAP.

We agree with the FASB’s conclusion that the application of the shortcut method is appropriate in circumstances when the trade date and settlement date of the hedged item are within the established conventions for the marketplace and when an interest rate swap has a non-zero fair value at inception due to the existence of a bid-ask spread between the entry transaction to purchase the swap and a hypothetical exit transaction. Conceptually, late hedging presents the same concern as the coupon rounding issue and the trade date settlement issue (both market conventions) that were deliberated by the FASB and addressed within the Exposure Draft. Both involve basis differences at inception; only, in late hedging, the amount of the premium or discount might be larger. We believe the Board should apply a consistent conclusion to all three of these issues and continue to allow the use of the shortcut method in all three instances.

The shortcut method was developed in response to cost/benefit concerns, and these concerns are still valid and in existence today. Prohibiting the use of the shortcut method for late hedges will increase the cost of implementing prudent risk management practices of infrequent debt issuers, like Exelon, and may have unintended consequences, such as encouraging some companies to enter into hedges sooner in order to qualify for shortcut treatment. Performing periodic effectiveness tests will increase the all-in cost of swaps, which we believe is not justified given that these hedging transactions are highly effective.

As hedge accounting is currently being evaluated broadly by the FASB, the issuance of the Exposure Draft is a short-term fix that will be more costly to registrants and the financial markets and is unnecessary. We would recommend that the FASB deliberate the issues addressed by the Exposure Draft in conjunction with its broader hedge accounting project as opposed to issuing interim guidance that would represent a major change in how the shortcut method is currently applied in practice to late hedges. We believe that the shortcut method has provided registrants with a cost-effective means of accounting for highly effective, extremely common transactions and would recommend that the FASB retain it, or a similar simplification, as part of its overall hedging project. Finally, if the Board ultimately votes to prohibit the application of the shortcut method to late hedges, we would recommend that the final guidance should, at a minimum, grandfather

existing hedging relationships given that the continued use of the shortcut method was allowable under FAS 133 when these transactions were initiated and executed.

Sincerely,

/s/ Matthew F. Hilzinger

Matthew F. Hilzinger  
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