September 3, 2010

Technical Director
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The Edison Electric Institute ("EEI") respectfully submits comments on the Financial Accounting Standards Board's ("FASB") Proposed Accounting Standards Update, Fair Value Measurements and Disclosures (Topic 820) – Amendments for Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs (Proposed Update). EEI is the association of U.S. shareholder-owned electric companies. Our members provide service to 95 percent of the ultimate customers in the shareholder-owned segment of the industry, and represent approximately 70 percent of the U.S. electric power industry. Our members hold a variety of commodity contracts to hedge the market and credit risk associated with the generation and distribution of electricity, as well as other assets and liabilities that are measured at fair value. Many of these contracts are considered derivative instruments under Topic 815, Derivatives and Hedging or available-for-sale investments under Topic 320, Investments – Debt and Equity Securities and must be recorded and disclosed at fair value. Therefore, EEI and our members have a direct interest in the Proposed Update.

Although we will be providing comments on certain provisions within the Proposed Update, we want to stress our overall support for this project to achieve convergence with International Financial Reporting Standards. We are in agreement with the core concepts of the Proposed Update, and any of the comments we have are secondary to our support for the project as whole. We welcome this opportunity to respond to the Proposed Update and address some of the questions raised by the Board.
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**Question 1**
*This Exposure Draft represents the Board's commitment toward developing common fair value measurement guidance with the IASB. Do you think the proposed amendments:*
  
a. Would improve the understandability of the fair value measurement guidance in U.S. GAAP? If not, why not?
  
b. Would result in any unintended consequences on the application of the proposed amendments? If so, please describe those consequences.*

While we believe the proposed guidance would improve the understandability of the fair value guidance, there is one unintended consequence we would like to highlight. We do not believe the proposed requirement to disclose “any” transfers between Level 1 and 2 will provide sufficient beneficial information to financial statement users to justify the administrative burden on preparers. Level 1 and 2 inputs are both based on observable inputs and transfers between these levels that are not significant will not be valuable to financial statement users. The current requirement to disclose significant transfers between Level 1 and 2 became effective January 1, 2010 due to *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures About Fair Value Measurements*. The Basis for Conclusions of that document states that this transfer information may be used by users in their assessment of the quality of reported earnings and expected future cash flows. We believe the disclosure of the ending fair value amount and level in which that amount is classified within the hierarchy, as well as Level 3 and significant Level 1 and 2 transfers, provide the most relevant information for users. Level 1 and 2 transfers that are not significant do not provide useful information related to the quality of earnings and should not be used to form an expectation about future cash flows. Many companies review their Level 1 and 2 classifications at the end of each quarter, and additional processes would need to be established to track insignificant transfer activity during the quarter. We propose that the current disclosure requirements regarding significant Level 1 and 2 transfers remain without change.

**Question 7**
*The Board has decided to require a reporting entity to disclose a measurement uncertainty analysis that takes into account the effect of correlation between unobservable inputs for recurring fair value measurements categorized within Level 3 of the fair value hierarchy... Do you think that proposal is appropriate? If not, why not?*

We believe the proposed measurement uncertainty analysis for fair value measurements categorized within Level 3 is significantly improved from the
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proposal in the Exposure Draft for Accounting Standard 2010-06 on Topic 820. In particular we were encouraged that the Basis for Conclusion clarified the following:

- Disclosure is not intended to reflect remote (including worst-case) scenarios  
- Disclosure is not meant to predict how a fair value measurement would change in the future because of changes in future economic conditions  
- Entities should not need to assess how observable inputs might have differed  
- Significance should be judged against earnings or total assets/liabilities  
- Disclosure is not meant to provide users of financial statements with information for second guessing a reporting entity’s fair value measurements

We also believe that the change in wording from ‘reasonably possible alternative inputs’ to ‘unobservable inputs…that could have reasonably been used in the circumstance’ helps to clarify the objective of the disclosure. The prior wording implied a much wider range of alternative inputs that would need to be considered, whereas the new wording implies that only alternative inputs that a market participant could have used in estimating fair value (i.e., could have been recorded in audited financial statements) should be considered.

While we recognize these improvements, we continue to be concerned that the measurement uncertainty analysis, as proposed, would not provide meaningful information and will be difficult to audit, given the inherent subjectivity of identifying potential alternative inputs for Level 3 fair value measurements, which themselves are the most subjective measurements in the fair value hierarchy. Additionally, we share the concerns of some Board members about the operationality of the proposed measurement uncertainty analysis disclosure and whether the benefit to users of financial statements would outweigh the additional cost to reporting entities for providing the disclosure on a quarterly basis.

We suggest that users cannot truly appreciate the results of a measurement uncertainty analysis without a detailed knowledge of how the measurements were prepared, which in our view represents a level of detail that is unreasonable to disclose in financial statements. For example, there are thousands of delivery points across the United States for power contracts, because power cannot be stored nor transported across large distances. Furthermore, the thousands of delivery points theoretically have forward prices that vary by region, season, and month, and these forward prices are influenced by the correlation to other energy products (power to gas, gas to expected gas storage volumes, gas to oil, oil to...
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emission allowances, etc.). Within PJM (a regional electricity market that encompasses all or part of thirteen states, primarily in the Mid-Atlantic), there are over 8,000 delivery points, but less than ten are actively traded and have observable forward prices. As such, it may not be feasible to prepare meaningful measurement uncertainty analyses based on other unobservable inputs that could have been reasonably used without being overly voluminous or using subjective selections.

Furthermore, the measurement uncertainty analysis proposed by the Exposure Draft is not currently available because it is calculated in a manner inconsistent with the tools management uses to assess its risks. Risk management activities appropriately use sensitivity analyses prepared at a portfolio level, in which all market-related risks and offsetting positions are evaluated together. As such, all assets and/or liabilities within a class are evaluated together with contracts that receive accrual accounting, as well as physical assets. We believe that other information can be disclosed that will provide users of financial statements with useful information about Level 3 fair value measurements that do not require the same subjectivity that would be required under the proposed guidance, and we discuss these alternatives in our response to Question 8.

However, if the Board decides to retain the proposed uncertainty analysis, we believe that it would be important to clarify the Board’s intentions regarding alternative methods for computing the disclosure. Additionally, we believe that the operationality of the proposal would be improved significantly if this clarification would address certain practical issues regarding the level at which the analysis should be performed.

We discuss our concerns below.

Application of Principles

The proposed requirements for the measurement uncertainty analysis are articulated in the form of principles and do not prescribe specific rules or mechanics for computation. While we concur that the use of principles, in theory, is more likely to result in useful financial information that is relevant and comparable, we also recognize that the transition to a principles-based environment in the United States is, at best, incomplete. In practice, there is often a desire to default to rules of thumb or to achieve uniformity as a way to minimize the responsibility for applying judgment.

We believe that the principles for the required measurement uncertainty analysis could be interpreted in a variety of ways that could result in different calculation
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methods and conventions. We believe that, to the extent that such approaches are consistent with the objectives of the Update, are applied consistently, and material aspects of the approach are disclosed, such good faith differences in approach should be considered appropriate.

We recommend that the Board include in the final Update an explicit statement acknowledging the possibility of alternative interpretations of these principles and different methods for evaluating and computing these disclosures. We also request the Board to clarify that no one approach is necessarily required as long as the approach selected produces a result that achieves the objectives of the Update, is applied consistently, and is fully disclosed. We believe that these clarifications will significantly reduce the possibility for conflict between preparers, users, and auditors of such disclosures and eliminate inefficient and unnecessary work in developing unofficial rules to standardize or create uniformity where no such requirement is present or intended.

Level of Analysis
We also believe that further clarification is needed as to the specificity of an input and how the determination of an input interacts with the definition of a fair value measurement and the classes of fair value measurements for which disclosure is required. While the discussion below reflects only one possible interpretation of the principles underlying the proposed update, we believe that addressing the issues raised by these comments would improve understanding of the principles in the proposed update. Accordingly, we recommend the following clarifications:

1) Indicating that the classes of fair value measurements disclosed in accordance with paragraph 820-10-50-2C may include a number of separate fair value measurements with similar types of unobservable inputs within each class;

2) Indicating that disclosure of the uncertainty analysis required by paragraph 820-10-20-2-f may apply to some, but not all, of the separate fair value measurements within a class because similar unobservable inputs may not always be subject to the same magnitude of potential variation;

3) Indicating that the disclosure is not intended to aggregate multiple individually insignificant sensitivity amounts if the underlying inputs are not correlated

We illustrate below the potential issues that give rise to our concerns and lead to these recommendations.

EEI members enter into derivative contracts to buy and sell power, natural gas and coal (and other commodities) in markets throughout the United States.
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Because power cannot be stored nor transported across long distances, the fair value of an individual power derivative contract is driven largely by the forward price curve for its specific regional delivery point. In our fair value disclosures, we often provide information for power contracts in total, which consists of an aggregation of the fair value of power derivatives in each region. Thus, while the fair value measurements included in the “power” disclosures class are subject to the same types of measurement uncertainties by their nature (for example, basis differences between liquid delivery points and illiquid delivery points), the aggregation of power contracts constitutes a meaningful class for which to provide disclosure.

We believe it is important to clarify that each class of disclosures appropriately may include multiple fair value measurements with similar types of inputs. As an illustration, the proposed Example 10 - Measurement Uncertainty Analysis on page 244 of the Proposed Update contains a single line for residential mortgage-backed securities and notes that one of the significant unobservable inputs is probability of default. However, it is unclear if the estimated fair value of all residential mortgage-backed securities included in the line is based on a single probability of default rate or if there are subcategories of securities that have unique default rates that have been aggregated to compile this disclosure.

Second, while a class of disclosures may include multiple fair value measurements that share similar types of inputs, the underlying inputs may not all vary based on the same factors or to the same degree. This is particularly true for physical commodities that may be quite similar in their fundamental nature but that can vary more substantially in value based upon physical location. For example, power contracts in one region are not necessarily subject to the same extent of variation as those in another region – one region may be more liquid and have fewer illiquid points, resulting in less measurement uncertainty, while another region may have less liquid points and lower transaction volume, resulting in a greater proportion of fair value inputs that require estimation.

Therefore, we believe it is important to clarify that such differences in the specific factors underlying a class of fair value measurements make it appropriate to evaluate the level of uncertainty in a way that responds appropriately in the circumstances. In some cases, the level of potential uncertainty of a portion of a class may be de minimis, another portion may be evaluated qualitatively, and yet another portion may require quantitative analysis.

Finally, we believe it would be helpful to clarify whether certain calculation mechanics would be consistent with the ASU’s objectives. One interpretation for
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computing the uncertainty analysis would be to compute the potential variation in 
fair value of each individual measurement (i.e., contract) and then to aggregate 
those amounts for disclosure. While this approach is more likely to yield an 
aggregate amount that would be considered significant, we believe that it is 
inconsistent with the principles of considering correlations and would serve to 
overstate the potential estimation error in the fair value measurements.

We believe it is more appropriate, and in fact is consistent with the requirement 
to consider correlation, to compute potential fair value measurement differences 
by aggregating concentrations or groups of fair value measurements that have 
both the same Level 3 inputs and for which those inputs would respond in a 
similar or correlated manner. While we believe that this reflects the spirit of the 
ASU and meets its objectives, our experience indicates that diversity in practice 
could result unless the final ASU clarifies this type of practical computational 
matter.

In order to illustrate our recommendations comprehensively, consider the 
following simple example that uses the total amounts from the table on page 244 
for residential mortgage-backed securities but changes the line item to power 
derivatives. The location is based on the different Regional Transmission 
Organizations (RTO) and Independent System Operators (ISO) in the United 
States. Also, for purposes of this example, materiality is judged to be $14 million 
based on total assets and earnings.

<table>
<thead>
<tr>
<th>Location</th>
<th>Fair Value at 12/31/09</th>
<th>Increase in Fair Value</th>
<th>Decrease in Fair Value</th>
<th>Significant Unobservable Input¹</th>
</tr>
</thead>
<tbody>
<tr>
<td>California</td>
<td>35</td>
<td>3</td>
<td>(2)</td>
<td>Forward prices in CAISO</td>
</tr>
<tr>
<td>Texas</td>
<td>20</td>
<td>6</td>
<td>(4)</td>
<td>Forward prices in ERCOT</td>
</tr>
<tr>
<td>Maryland</td>
<td>10</td>
<td>4</td>
<td>(2)</td>
<td>Forward prices in PJM</td>
</tr>
<tr>
<td>Nebraska</td>
<td>40</td>
<td>8</td>
<td>(7)</td>
<td>Forward prices in SPP</td>
</tr>
<tr>
<td>Illinois</td>
<td>20</td>
<td>3</td>
<td>(3)</td>
<td>Forward prices in MISO</td>
</tr>
<tr>
<td><strong>Total Power Derivatives</strong></td>
<td><strong>125</strong></td>
<td><strong>24</strong></td>
<td><strong>(18)</strong></td>
<td></td>
</tr>
</tbody>
</table>

¹ The acronym in each case represents the regional RTO/ISO.

In this example, it is clear that the single class of power derivatives is made up of 
contracts for the same underlying commodity that include the same type of 
unobservable input. The primary difference between the inputs is the specific
physical location, not its underlying nature. This is typical of power derivative disclosures in our industry, and we believe that it is appropriate.

Note also, consistent with our second observation above, that the variation in fair value that would be computed for each region differs in absolute and percentage terms. Depending upon the factors underlying the region, the extent to which prices were observable, and the relative volatility in each region, some of these potential changes in fair value could, in practice, easily be identified as not significant without making specific calculations. Again, we believe that this is appropriate and that the final ASU should clarify that this approach constitutes a reasonable exercise of judgment.

Finally, we believe the only necessary sensitivity analysis disclosure that would be required would be for the power derivatives located in the Southern Power Pool (SPP), because the potential change in fair value of $15 million (i.e., the range) is material. We would not show the aggregated amounts of $24 million and $(18) million, because they are based on the sum of the insignificant impact of different individual inputs that are not correlated or otherwise related. Power prices in individual regions are based on local supply/demand in that region and are not correlated across the entire country. Simply aggregating the insignificant changes by region would imply a variability that could only be considered remote and/or worst case, both of which are inconsistent with the principles for this disclosure. In order to avoid doubt and potential disparity in application, we believe that it would be beneficial for the final ASU to clarify the application of its requirements as noted above.

Question 8
Are there alternative disclosures to the proposed measurement uncertainty analysis that you believe might provide users of financial statements with information about the measurement uncertainty inherent in fair value measurements categorized within Level 3 of the fair value hierarchy that the Board should consider instead? If so, please provide a description of those disclosures and the reasons why you think that information would be more useful and more cost-beneficial.

We struggle with the cost-benefit rationale for preparing the measurement uncertainty analysis associated with Level 3 classifications as we do not currently capture this information for purposes of reporting to our own management, including the chief decision maker. We believe the fair value of the instrument, coupled with the market risk disclosures and a statistical measure such as value at risk (VaR) and economic value at risk (EVaR), provides the most relevant
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information to investors. The fact that an instrument is classified as Level 3 already communicates to the reader that there is measurement uncertainty in valuing the instrument. However, we note it is possible that a significant portion (potentially up to 90%) of the instrument's fair value could be based on observable inputs. Thus, as an alternative, the measurement uncertainty analysis could be replaced by a requirement to disclose the percentage of the fair value that is based on unobservable inputs.

Consider a simple example where Company A holds a derivative contract that will financially settle over three years based on the movement in power prices at a particular location, but the forward price curve is observable for only two years. Ignoring discounting, 67% of the fair value is based on observable inputs and 33% is based on unobservable inputs (i.e., expected power prices in the third year), which results in the entire fair value being classified as Level 3. In contrast, assume Company A holds a similar derivative contract at a non-liquid delivery point, and thus none of the forward years are observable. Disclosing the percentage of fair value that is based on unobservable inputs provides the user with additional information on the relative observability of the Level 3 measurements. We believe many companies would be able to readily provide this information as they have current processes to determine whether a contract should be classified as Level 2 or Level 3.

In our industry, a significant amount of recurring fair value measurements are financial or physical commodity derivative contracts. The derivatives are generally held for economic hedging purposes and often qualify for hedge accounting treatment. The hedged items are often forecasted transactions related to non-derivative contracts and physical assets whose fair value would likely also be considered a Level 3 measurement. Measurement uncertainty should be less of a concern for instruments held for hedging purposes since the fair value measurements would be at least partially offset by measurement uncertainty with regard to the hedged item. Another alternative disclosure, albeit only related to derivatives, would be to disclose the amount of Level 3 fair value measurements that are in hedging relationships, are considered economic hedges, or represent proprietary trading activities.

Question 12
How much time do you think constituents would need to prepare for and implement the amendments in this proposed Update?
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Except for the uncertainty analysis, many of the amendments to Topic 820 are not significant and will take no longer than six months to implement. The measurement uncertainty analysis will take a significant amount of time to accumulate and analyze the data required to be disclosed. As noted above, this information is not currently available, because management does not currently use this type of analysis. As such, the adoption of this provision will require system modifications or manual workarounds. Should the Board adopt the provisions, we recommend that the implementation date coincide with the implementation date that is established for the Proposed Accounting Standards Update—Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities—Financial Instruments (Topic 825) and Derivatives and Hedging (Topic 815), in order to minimize the impact of system design changes and subsequent testing.

Summary

We appreciate your consideration of this issue and our comments. We believe the issuance of these amendments and clarifications to the fair value measurement guidance will be a significant benefit to financial statement users, preparers and regulators. However, we believe the cost to prepare the measurement uncertainty analysis outweighs the benefit to users and therefore recommend that the Board either remove this requirement or consider alternative approaches.

Very truly yours,

[Signature]

David K. Owens