Dear Mr. Golden:

FirstEnergy Corp. appreciates the opportunity to share our thoughts on the proposed Statement 133 Implementation Issue E23.

FirstEnergy Corp. is a diversified energy company with $32 billion of assets and nearly $12 billion in annual revenues. Our electric utility operating companies comprise the nation's fifth largest investor-owned electric system, serving 4.5 million customers within 36,100 square miles of Ohio, Pennsylvania and New Jersey; our generation subsidiaries control more than 14,000 megawatts of capacity.

As a user of derivative instruments, many of which are documented as cash flow hedges or fair value hedges under Statement 133, we strongly support the Financial Accounting Standards Board's (FASB) project to review hedge accounting. Many of the intricacies involved in qualifying for hedge accounting and the effectiveness testing required are highly complex, which we believe from our experience creates an incomprehensible accounting model of questionable value to many financial statement users. We concur that the proposed Issue E23 should remedy some of that complexity, contributing to the overall goal of the hedging project.

We agree that the proposed Issue E23 will clarify that both the fixed and variable legs of a swap must have notional values equal to the hedged item over the lifetime of the hedge relationship in order to qualify under paragraph 68 of Statement 133 (commonly known as the "shortcut method"), as well as clarifying that swaps with non-zero fair values at inception may use the shortcut method when that value is due to the bid-ask spread. However, FirstEnergy is concerned with the FASB's interpretation that a hedging relationship created subsequent to the recognition of the hedged item invalidates the assumption of no ineffectiveness and therefore disallows use of the short cut method.

The proposed elimination of the shortcut method for what are being called "late hedges" appears to be inconsistent with current Statement 133 guidance and may deter companies from protecting against a real risk in order to avoid the complicated and time-consuming documentation currently under review in the hedging project. FirstEnergy, like many companies, uses interest rate swaps to protect against interest rate fluctuations that drive the change in the fair value of debt. We believe that the inception date of an interest rate swap does not impact the underlying economic impact of the swap and its relationship to the hedged item. Proposed Issue E23 cites the non-par fair value of the debt as the rationale for disallowing the short cut method, stating that non-par indicates a higher or lower yield than that which exists with par debt, which would not be offset by a swap. Those prospective changes in fair value, however, are driven by movement of the underlying interest rate which are offset by a swap; the recognition of discounts or premiums to recognize the varying yield of the debt are the result of the mixed model accounting environment and not the ineffectiveness of the hedge relationship.
From the perspective of a financial report user, there is little difference between a hedge relationship created using an interest rate swap at the inception date or at a later date, and the existence of dissimilar procedures creates confusion. Furthermore, the discussions surrounding the ongoing hedging project indicate that effectiveness testing may no longer be required; it is counterintuitive to require hedges that have been elected previously without effectiveness testing to require contemporaneous effectiveness testing when the practice as a whole is being reconsidered. Requiring additional and complex testing for a late hedge results in unnecessary uses of a company's resources with no change in the effectiveness of the hedge relationship.

FirstEnergy looks forward to continuing participation in this important hedging project. We believe the end result should be a manageable accounting model that improves financial reporting by providing useful and understandable information about entities' hedging activities to all users of financial statements.

Sincerely,

Harvey L. Wagner
Vice President, Controller and Chief Accounting Officer
FirstEnergy Corp.

HLW:dc