April 22, 2013

Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

File Reference No. EITF 13-A, Proposed Accounting Standards Update – Derivatives and Hedging (Topic 815), Inclusion of the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) as a Benchmark Interest Rate for Hedge Accounting Purposes

Dear Technical Director:

The PNC Financial Services Group, Inc. (‘‘PNC’’) appreciates the opportunity to comment on the Proposed Accounting Standards Update – Derivatives and Hedging (Topic 815), Inclusion of the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) as a Benchmark Interest Rate for Hedge Accounting Purposes, (‘‘the Proposed ASU’’) which proposes guidance to permit the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate (‘‘OIS’’)) to be included as a U.S. benchmark interest rate for hedge accounting purposes under Topic 815.

We agree that OIS should be included as a U.S. benchmark interest rate for hedge accounting purposes under Topic 815, in addition to the interest rates on direct Treasury obligations of the U.S. government (‘‘UST’’) and the London Interbank Offered Rate (‘‘LIBOR’’) swap rate. We also agree that no additional disclosures should be required. Additionally, we believe that the effective date of the amendments in the Proposed ASU should coincide with the issuance date of the final ASU.

We are concerned that the ability to designate OIS as a benchmark interest rate in hedging relationships under the Proposed ASU may conflict with the existing guidance in ASC 815-20-25-6 which indicates that ‘‘...[o]rdinarily, an entity shall designate the same benchmark interest rate as the risk being hedged for similar hedges, consistent with paragraphs 815-20-25-80 through 25-81. The use of different benchmark interest rates for similar hedges shall be rare and shall be justified...’’ We encourage the Emerging Issues Task Force (‘‘EITF’’) to consider the interrelationship between the proposed guidance and this existing requirement, and recommend the removal of the restriction that the use of different benchmark interest rates for similar hedges shall be rare. Given that we may manage risk differently across different products, risk managers should have the ability to designate whether LIBOR or OIS is best suited for a specific hedging relationship. Consider the following example which we believe would justify the potential use of different benchmark interest rates based upon the relative pricing of a swap for similar hedging relationships:
PNC forecasts it will issue a five-year, fixed rate bond in 6 months at the market rate at the time of issuance. PNC's treasury unit (i.e., risk manager) would like to hedge the variability in cash flows caused by changes in interest rates up to the date of issuance, using a forward starting swap. The treasury unit does not anticipate that the OIS-LIBOR basis will fluctuate significantly over the next 6 months and is therefore neutral to using either an OIS or LIBOR-based swap. Based on pricing terms, a forward starting OIS-based swap is selected for this particular hedging relationship. In the future for other forecasted debt issuances, the treasury unit may find the forward starting LIBOR-based swap to be a better hedging instrument based on pricing and effectiveness determinations.

**Hedge Effectiveness Testing and Ineffectiveness Measurement**

While not explicitly addressed in the Proposed ASU, we request the EITF expand the transition guidance to permit the use of OIS as the discount rate for determining fair value in existing hedge relationships. PNC, as well as other financial services companies, have existing documented accounting hedge relationships in which the hedged risk is based on LIBOR. As the principal market is converting to the use of OIS discounting in swap valuations, the fair value accounting guidance requires us to value our hedging instruments (i.e., swaps) using OIS discounting. However, the linkage between the fair value and hedge accounting guidance would then result in fair valuing the swaps inconsistently with the original hedge documentation. Furthermore, if the swaps are valued using OIS discounting, it is logical to also value the hedged item using OIS discounting so that artificial ineffectiveness is not created by changes in the basis between OIS and LIBOR since we expect the hedges to remain highly effective. Since our existing hedge documentation references use of LIBOR as the discount rate in effectiveness testing and ineffectiveness measurement, modifying the documentation to incorporate OIS discounting may result in redesignation of the existing hedge relationship and establishment of a new hedge relationship with an off-market swap.

Alternatively, we believe the transition guidance should recognize the relationship with the guidance in ASC Topic 820, *Fair Value Measurement* and permit entities to modify their existing hedge documentation for the use of OIS discounting for purposes of assessing hedge effectiveness and determining hedge ineffectiveness without causing a new hedge relationship to be created. Without this ability to switch to the use of OIS discounting in accounting hedges, companies are faced with either breaking existing hedges, which will be uneconomical and operationally inefficient, or in the case of the swap and hedged item being discounted at different rates, recording unnecessary ineffectiveness in the financial statements to the extent OIS and LIBOR move asymmetrically. Should the movement in the OIS-LIBOR basis be significant, it could also cause the hedge to fail the effectiveness testing, thereby creating accounting exposure and volatility in earnings. Our existing hedges have been highly effective in hedging the designated risk, and we believe either of the above-mentioned outcomes would result in a punitive consequence of having to determine the fair value of the swap using OIS discounting and value the change in the hedged item using LIBOR. The resulting volatility would not provide meaningful information to a financial statement reader since the hedge relationships will continue to be highly effective in hedging their designated risks.

Lastly, we encourage the EITF to consider practical implications of using OIS discounting in hedge effectiveness testing and ineffectiveness measurement. OIS has increased in prevalence in the marketplace since 2008 and as a result, for existing hedges that have been in place since
before 2008, there are not sufficient reliable historical data for OIS rates to use OIS discounting for all retrospective data points since the inception of those hedges. Therefore, we recommend that OIS discounting be implemented for existing hedges for purposes of determining data points to be incorporated into hedge effectiveness testing by beginning to use OIS discounting to value both the hedge and hedged item in current and prospective effectiveness testing data points.

**********

We appreciate the FASB’s request for feedback on this matter and appreciate the opportunity to share our views with the Board and staff. We welcome any questions or comments you may have. Please contact me with any questions about PNC’s comments at 412-762-7546.

Sincerely,

John (JJ) Matthews
Director of Accounting Policy
The PNC Financial Services Group, Inc.

cc: Mr. Richard Johnson
Executive Vice President and Chief Financial Officer
The PNC Financial Services Group, Inc.

Mr. Gregory Kozich
Senior Vice President and Controller
The PNC Financial Services Group, Inc.